# DLA

## FISCAL YEAR 2023

# Defense Logistics Agency

## AGENCY FINANCIAL REPORT

- Working Capital Fund
- General Fund
- National Defense Stockpile Transaction Fund

# Defense Logistics Agency

## FY 2023 | AGENCY FINANCIAL REPORT

*The Nation's Combat Logistics Support Agency*

**The Defense Logistics Agency (DLA) Headquarters**

The Defense Logistics Agency (DLA) headquarters, also known as the Andrew T. McNamara Headquarters Complex, at Fort Belvoir, Virginia. The headquarters contains numerous offices responsible for supporting the overall agency. DLA provides supplies to the military services and supports their acquisition of weapons, fuel, repair parts, and other materials. The agency also disposes of excess or unusable equipment through various programs.

**Andrew T. McNamara Building** | 8725 John J. Kingman Road Fort Belvoir, VA 22060-6221

# About the Agency Financial Report

The Defense Logistics Agency (DLA) Agency Financial Report (AFR) includes three reporting entities: Working Capital Fund (WCF), General Fund (GF), and National Defense Stockpile Transaction Fund (NDSTF). The AFR provides financial and summary performance results enabling the President, Congress, and the American people to assess its accomplishments, and to understand its financial results and operational functions. The AFR consists of DLA WCF, GF, and NDSTF financial statements and other reports. The principal financial statements[1] have been prepared to report the financial position and results of DLA WCF, GF, and NDSTF's operations. The principal financial statements and accompanying notes have been prepared from the books and records of DLA WCF, GF, and NDSTF using guidance from the following applicable laws and regulations for which DLA is unable to provide assurance:

- Federal Managers' Financial Integrity Act (FMFIA) of 1982;
- Chief Financial Officers (CFO) Act of 1990;
- Government Management Reform Act (GMRA) of 1994;
- Federal Financial Management Improvement Act (FFMIA) of 1996;
- Reports Consolidation Act of 2000;
- Government Performance and Results Act (GPRA) Modernization Act of 2010;
- Payment Integrity Information Act of (PIIA) 2019
- Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, as amended;
- OMB Circular A-123, Management's responsibility for Enterprise Risk Management (ERM) and Internal Control; and
- OMB Circular A-11, Preparation, Submission, and Execution of the Budget.

DLA WCF, GF, and NDSTF's financial results are unaudited because there are limitations due to underlying processes and internal controls that support the principal financial statements. DLA continues to implement processes and system improvements addressing these limitations. The AFR consists of three primary sections:

### Management's Discussion and Analysis (Unaudited)

This section provides a high-level overview of DLA WCF, GF, and NDSTF, including DLA's history, mission, and organizational structure; DLA WCF, GF, and NDSTF's overall performance related to its strategic goals and primary objectives; financial analysis; management's assurance on internal controls; system analysis; compliance with laws and regulations; and forward-looking information.

### Financial Section (Unaudited)

This section contains a message from the CFO and DLA WCF, GF, and NDSTF audit reports, management's response to the audit reports, financial statements and the accompanying notes, as well as required supplementary information (RSI) (DLA WCF and GF only).

### Other Information (Unaudited)

This section details DLA's compliance with, and commitment to, specific regulations. It includes Summary of Financial Statement Audit and Management Assurances, DLA WCF revenue forgone reporting, management and performance challenges, and payment integrity reporting.

[1] Refer to the Financial Section Introduction for definition of principal financial statements.


## Supply Delivery

An Army CH-47F Chinook assigned to the 1st Armored Division Combat Aviation Brigade delivers relief supplies to Pazarcik, Turkey, Feb. 15, 2023. **Photo By:** Army Spc. William Thompson

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# Message from the Director

## FY 2023 | AGENCY FINANCIAL REPORT

On behalf of the Defense Logistics Agency (DLA), I am pleased to present the Fiscal Year (FY) 2023 Agency Financial Report (AFR). For the past sixty-two years, DLA has vigilantly focused on serving the Warfighter, and remaining a dynamic and forward-leaning Agency with vast capabilities, fueled by a dedicated and mission-focused workforce. As DLA continues through its seventh decade, we remain "Forged by History, Focused on the Future," and proud to serve as the Nation's Combat Logistics Support Agency.

DLA continued to fulfill our key mission to deliver readiness and lethality to the "Warfighter Always," and to provide support to our Nation through quality, proactive global logistics. We have continued to adapt our efforts as needed throughout every competitive, operational environment in which we operate. From boots on the ground to the space domain, DLA is ever present. In FY 2023, DLA had $1.3B in sales to the Department of Health and Human Services for COVID-19 response. DLA continues to support the Department of the Navy in defueling the Red Hill Bulk Fuel Storage Facility, including restoring access to safe water, supporting affected families, emergency defueling and fuel dispersal, obligating $764.3M in FY 2023.

This year, our Independent Public Accounting (IPA) firm, Ernst and Young, LLP, issued a Disclaimer of Opinion on DLA's Working Capital Fund (WCF), General Fund (GF), and National Defense Stockpile Transaction Fund (NDSTF) AFR. Information obtained through this report will be valuable in our ongoing efforts to improve all aspects of DLA's operations. The IPA reported material weaknesses in key areas involving policies and procedures, critical asset accounting procedures, financial information systems, reporting, and completeness of records. DLA continues to track and remediate material weaknesses in these areas.

DLA's audit roadmap to unmodified opinions is focused on process improvements, strengthened financial management, and improved monitoring and oversight. DLA's efforts have increased accountability, communication, and support across all levels of the organization to better focus our attention and align resources to areas with the most critical need and potential impact. DLA fully supports the overall Department of Defense priorities to deliver transparent financial reporting with integrity and agility in support of the National Defense Strategy. DLA will review audit results, identify root causes, prioritize resources, and develop corrective action plans. This effort will rely on continued identification of risks and establishing effective internal

***DLA*** *continued to fulfill our* ***key mission*** *to deliver* ***readiness*** *and* ***lethality*** *to the* ***"Warfighter Always,"*** *and to* ***provide support*** *to our Nation through* ***quality, proactive global logistics.***

controls throughout every process. DLA is reviewing all aspects of OMB Circulars A-123, Management's Responsibility for Enterprise Risk Management and Internal Control, and A-136, Financial Reporting Requirements, to incorporate necessary enterprise-wide operational and financial reporting process changes that will ensure our financial statements are complete, accurate, and reliable.

As always, I am proud of our legacy and our mission, "…to provide effective logistics support to the operating forces of our military services and do so at the lowest possible cost to the taxpayer." With this report, we reaffirm our commitment to supporting our Warfighters and our Nation through efficient and accountable resource management and making strides toward stronger fiscal transparency and performance.

M.C. SKUBIC
VADM, SC, USN
**DIRECTOR**

## WARFIGHTERS ALWAYS


DEPARTMENT OF DEFENSE
UNITED STATES OF AMERICA

# Section 1

# *Management's Discussion and Analysis*

(Unaudited)

◀ **Marine Corps - DLA Day**

Defense Logistics Agency and Marine Corps leaders met May 1 at DLA's Fort Belvoir, Virginia, headquarters to discuss strategic issues and ensure DLA support is aligned with customer priorities during Marine Corps-DLA Day.

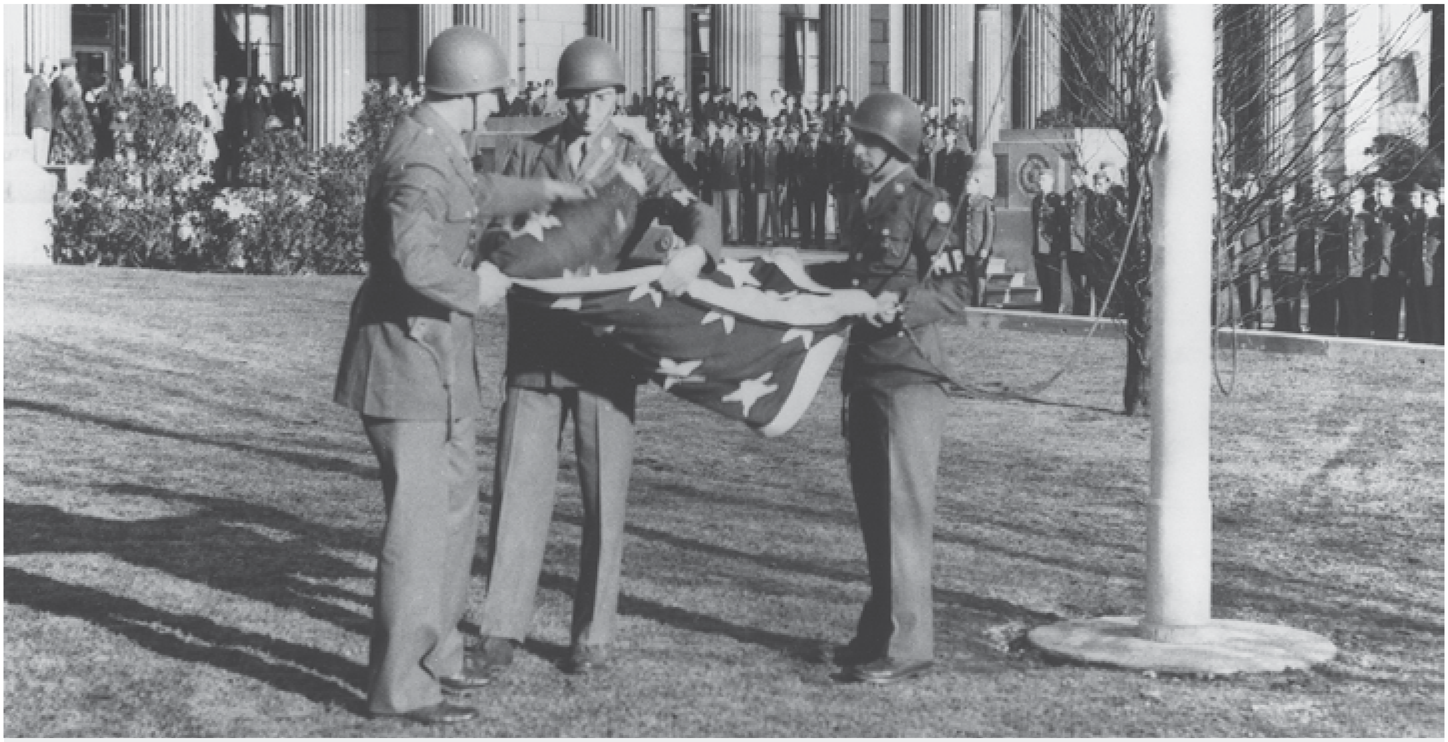
**Photo By:** Christopher Lynch

# Section 1

## *Management's Discussion and Analysis* (Unaudited)

## In this section:

# Mission and Organizational Structure



**DLA Disposition Services**

January 15, 1943, the US Army held its first flag raising ceremony at the Percy Jones Army Hospital, Battle Creek, Michigan. It would go on to become the largest Army Hospital during World War II. Today the building is home to DLA Disposition Services headquarters.

**Photo by:** courtesy of DLA

## Forged by History, Focused on the Future:

*A Short History of the Defense Logistics Agency*

The origins of DLA date back to World War II when America's military buildup required the rapid procurement of vast amounts of supplies. After the war, a commission headed by former President Herbert Hoover recommended the central management of items common to more than one military service. The Department of Defense (DoD) responded by assigning procurement responsibilities to individual services. The Army became the military's sole buyer of food, clothing, general supplies, and construction supplies; the Navy purchased medical supplies, petroleum, and industrial parts for every service; and only the Air Force provided airlift services.

Although centralizing wholesale stocks, this "single manager" system did not provide the uniform methods recommended by the Hoover Commission. Each single manager operated under its own rules, giving customers as many sets of procedures as there were managers. On October 1, 1961, Secretary of Defense Robert McNamara eliminated this complexity by forming the Defense Supply Agency (DSA). Beginning operations on January 1, 1962, DSA saved money by employing fewer people and keeping less inventory.

DSA faced its first real-world test one year after formation. Restricted to the continental United States, it was perfectly positioned to respond to Soviet Premier Nikita S. Khrushchev's placement of nuclear missiles on Cuba. The Agency supported the military by supplying fuel and photographic film and the Nation after it by providing fallout shelter material.

DSA grew substantially following the Cuban Missile Crisis. In 1963 and 1964, it assumed control of additional warehouses and supply centers. In 1965, it consolidated contract management offices under its Headquarters (HQ). Through its Defense Contract Administration Services (DCAS), DSA oversaw most of the Nation's defense contractors, as well as companies manufacturing items for the National Aeronautics and Space Administration (NASA).

The war in Vietnam also fueled DSA's growth. In the summer of 1965, the clothing and textile supply chain doubled its employees to produce enough warm-weather uniforms and jungle boots for the 44 battalions deployed by President Lyndon B. Johnson. Warehouses also increased hiring, adding shifts so they could operate on a 24-hour schedule. When the subsistence supply chain received permission to establish offices in the Pacific, it increased its numbers as well.

DSA received additional responsibilities Outside the Continental United States (OCONUS) in the last years of the war. In 1972, it started conducting property disposal overseas and oversaw the worldwide procurement, management, and distribution of bulk petroleum. In 1973, it began providing food to mess halls and commissaries in Europe. At the same time, the Agency became involved in foreign military sales (FMS). The weapon systems America sold to partner nations needed repair parts, and DSA was the logical provider.

On January 1, 1977, the Department of Defense recognized this expanded mission by renaming DSA the Defense Logistics Agency. Over the next decade and a half, the retitled Agency demonstrated its acquisition prowess by acquiring meals, ready-to-eat; filling the Nation's Strategic Petroleum Reserve; and providing parts for the F-16 Fighting Falcon, the most manufactured fighter jet in history. Parts production reached all-time highs with the Reagan buildup of the 1980s. In 1986, DLA grew in purpose and scope when Congress designated it a combat support Agency. In 1988, it became even more important to DoD when the General Services Administration (GSA) transferred strategic materials oversight to it. The following year, the Department consolidated nearly all contract administration activities under the Agency. To handle the increased workload, DLA elevated DCAS to a command: the Defense Contract Management Command (DCMC).

A robust contract management capability proved indispensable after Iraq invaded Kuwait in 1990. While DCMC revitalized an industrial base weakened by the end of the Cold War, the rest of the Agency housed, fed, equipped, and fueled a 500,000-person force in an austere land. In all, DLA processed 1.7 million requisitions, shipped $32.0 billion in spare parts, and contracted for $4.6 billion more: exemplary support that earned it its first joint unit meritorious award.

The Agency continued reorganizing after troops returned home. In April 1990, DoD gave DLA the mission of overseeing services' distribution depots. This mission eventual-

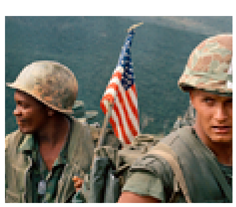
# History of DLA

**1961**

The DSA is established.


**1965**

Active combat units deploy to Vietnam. By 1969, more than 500,000 U.S. troops in the country.

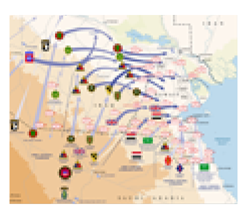


**1977**

DSA is redesignated the Defense Logistics Agency in recognition of its broadened mission responsibilities.

**1986**

The Goldwater-Nichols Reorganization Act designates DLA a combat support Agency.



**1988**

DLA assumes management of the nation's strategic stockpile from the General Services Administration and Federal Emergency Management Agency. Headquarters and Defense Fuel Supply personnel learn that they will be moving from Cameron Station to Fort Belvoir.

ly became the responsibility of DLA Distribution. In March 1993, the Agency reengineered its HQ so only 6 organizations, rather than 42, reported directly to the Director. In 1995, as a result of Base Realignment and Closure (BRAC) 88, DLA HQ moved from Cameron Station, VA, to Fort Belvoir, VA. In the mid-1990s, as a result of BRAC 93, the Agency merged its Defense Electronic Supply Center in Dayton, OH, with its Defense Construction Supply Center in Columbus, OH. It called the consolidated center Defense Supply Center Columbus. As part of the same BRAC, the Defense Personnel Support Center collocated with Defense Industrial Supply Center in northern Philadelphia to form Defense Supply Center Philadelphia. Finally, Defense Automated Publishing Service (formerly Defense Automated Printing Service), transferred to the Agency in October 1996.

The DLA rose to meet new challenges in the new millennium. The Agency responded rapidly to terrorist attacks in 2001, providing logistical support to multiple commands in Operation Enduring Freedom. For the next thirteen years, it strengthened lines of communication, provided material for base construction, provisioned dispersed units, and disposed of equipment. When the U.S. launched Operation Iraqi Freedom in March 2003, DLA processed 6.4 million requisitions worth more than $6.9 billion, provided 180.5 million field meals, supplied nearly 2.0 million humanitarian daily rations, and sourced more than 3.0 billion U.S. gallons of fuel. It continued to serve customers through the surge, surge recovery, and withdrawal.

The DLA supported humanitarian and relief missions in addition to military operations in the twenty-first century. In August 2005, it offered food, fuel, and housing to the many Louisianians displaced by Hurricane Katrina. In October and November of 2012, it offered the same services to victims of Hurricane Sandy, one of the worst weather events to strike the eastern coast of the United States. In September 2014, it helped the U.S. Agency for International Development combat the deadly Ebola virus in West Africa, not only providing material but also developing the sustainment footprint. In the later part of the decade, DLA delivered disaster relief to Haiti and the Southeastern U.S., sustained Iraqi and Syrian refugees, helped the U.S. Forest Service fight fires, and provided resources to secure the Nation's southern border.

Since early 2020, DLA WCF has supported the Nation's efforts to fight COVID-19, its most-sustained non-military mission in 60 years. Through the Federal Emergency Management Agency (FEMA), Department of Health and Human Services (HHS), U.S Army Corps of Engineers (USACE), and military hospitals, the Agency provided personal protective equipment (PPE), ventilators, food, construction material, and repair parts. Among those DLA helped were inhabitants of hard-hit cities, residents of assisted-living facilities, and school children. In addition to supplying mass quantities of scarce goods at low prices, the Agency developed domestically sourced face masks, used additive manufacturing to produce face shields, and tracked PPE data for the entire Federal government. Starting in December 2020, it began distributing vaccines to the military's overseas locations.

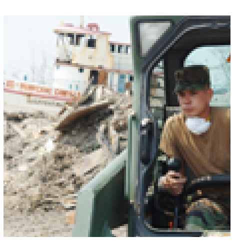
DLA continues to provide logistics, acquisition, and technical services to DoD and other customers and adds effectiveness and efficiency to governmental logistics.

**1993**

DLA forms integrated business units for supply management, distribution, and contract management, reducing the number of organizations reporting directly to the DLA director from 42 to 6.

**2005**

DLA provides support in the wake of Hurricane Katrina.



**2012**

DLA delivers more than 6.2 million meals, 172,500 blankets, and 14 million gallons of fuel to areas affected by Hurricane Sandy.

**2014-15**

DLA helps West Africa combat the Ebola virus by providing goods and services in Operation United Assistance.

**2020-23**

DLA supports efforts to combat the coronavirus by providing personal protective equipment and ventilators to the American people through the Federal Emergency Management Agency and Department of Health and Human Services. It also acts as a purveyor of information, feeds naval crews on lockdown, reutilizes life-saving equipment, and delivers vaccines to the military's overseas locations.

**The DLA's mission and vision are integral parts of the Agency which are represented through its efforts and impact around the world.**

**Photo By:** U.S. Army, Mark Cleghorn

## Mission

Deliver readiness and lethality to the Warfighter Always and support our Nation through quality, proactive global logistics.

## Vision

As the Nation's Combat Logistics Support Agency and valued partner, we are innovative, adaptable, agile, and accountable – focused on the Warfighter Always.

# What DLA Does

The DLA reports to the Office of the Under Secretary of Defense (OUSD) for Acquisition and Sustainment through the Assistant Secretary of Defense for Sustainment. As the Nation's Combat Logistics Support Agency, DLA manages the global supply chain – from raw materials to end user to disposition – for the components of the DoD (including the U.S. Army, Navy, and Air Force), other Federal Agencies, and public entities. DLA sources and provides nearly all the consumable items America's military forces need to operate, from food, fuel and energy to uniforms, medical supplies, and construction material. DLA provides support around the clock and around the world to meet the needs of America's Armed Forces and other designated customers in times of peace, national emergency, and war. DLA supports DoD objectives and missions with involvement in the full range of military operations from participation with multinational forces engaged in large-scale combat operations, weapons and spares provisions, peacekeeping efforts, and emergency support to humanitarian assistance.

The DLA WCF employs approximately 23,650 civilian personnel, 550 active-duty military personnel, and 650 reserve personnel, who operate a global enterprise in 20 countries and 47 states. Civilian personnel are paid from DLA WCF while active-duty military personnel and reserve personnel are paid from their respective Military Departments.

The DLA GF employs approximately 150 civilian personnel, whose labor is paid from DLA GF.

The DLA NDSTF employs approximately 50 civilian personnel, whose labor is paid from DLA NDSTF.

The National Defense Authorization Act (NDAA) is the U.S. Federal law specifying annual budget and expenditures of the DoD.

# How DLA Accomplishes its Mission

## Working Capital Fund

As part of fulfilling the government's duty to be publicly accountable for budgetary resources, DLA WCF maintains accountability primarily through contract authority for its operating and capital programs, as it relates to its two major activity groups: Energy and Supply Chain Management (SCM). DLA WCF rigorously plans, executes, and monitors budgetary resources, sales patterns, and rates of obligation in excess of $58.2 billion annually, while ensuring its mission of supplying American Warfighters with critical support. These resources are utilized in accordance with prevailing laws and regulations.

The DLA WCF has three major activity groups: Energy, SCM, and Document Services. Energy and SCM collaborate with Distribution and Disposition Services to form the six Major Subordinate Commands (MSCs) (as depicted in Figures 1 and 3). The Energy activity group manages the Energy MSC, and the SCM activity group manages the other five MSCs. The term MSC was devised by DLA's Director to reflect the flow of acquiring supplies, distributing supply materials, and disposing of excess supplies. In its support role, Distribution provides worldwide storage and distribution services to the eight supply chains described in Figure 1, while Disposition Services partners with DLA WCF's supply chains, DoD components (including the U.S. Army, Navy, and Air Force), other Federal Agencies, and public entities to reutilize, transfer, sell, and donate surplus property and dispose of hazardous waste.

The third DLA WCF activity, Document Services, operates primarily through spending authority from offsetting collections and outside of the MSCs. Its role is to provide preferred DoD document and printing services, as well as provide those services to other Federal Agencies.

The DLA WCF manages eight supply chains through the Energy and SCM activity groups and supports approximately 2,450 weapon systems. The eight supply chains are: Aviation, Land, Maritime, Fuel/Energy, Subsistence, Medical, Clothing and Textiles (C&T), and Construction and Equipment (C&E). In FY 2022, the Industrial Hardware (IH) national stock numbered items and workload were divided between Aviation, Land, and Maritime. The Energy activity group manages the Energy supply chain, and the SCM activity group manages the other seven supply chains. 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. Organizing as a single, integrated business enterprise enables DLA WCF to focus on supporting DoD components, other Federal Agencies, and public entities, enhancing the Armed Forces' readiness, and providing for the Warfighter during contingency operations.


**Figure 1:** DLA MSC Chart

# The DLA WCF has three major activity groups:
## *Energy, SCM, and Document Services*

The three major activity groups are described below:

### Energy

The DLA Energy activity group provides the DoD components (including the U.S. Army, Navy, and Air Force), other Federal Agencies, and public entities with comprehensive energy solutions worldwide. To do so, DLA Energy manages the Energy supply chain for energy-related products and services from jet fuel and natural gas to quality assurance and utility services, and many more. DLA Energy manages the following major product areas: Aerospace Energy, Bulk Petroleum Products, Direct Delivery Fuels, and Installation Energy. Additionally, DLA Energy provides services such as Government Fuel Cards, quality-related services, international fuel agreements, utility services contracts, and research and development (R&D) of alternative fuels to customers.

### Supply Chain Management

The DLA SCM activity group is responsible for managing seven supply chains and associated weapons systems. DLA SCM also provides logistics and material process management policy, guidance, and oversight while conducting continuous assessments of supply chain performance. DLA SCM integrates strategic, operational, and tactical perspectives, command and control functions for contingency operations, and adaptive planning in order to influence the logistics supply chain. Additionally, DLA SCM operates a global network of distribution centers and Disposition Services for reutilization, transfers, and donations. DLA WCF's warehousing strategy is driven by the commitment to better serve Warfighters, collocating with the Armed Forces while placing supplies where they are most needed.

### Document Services

Operating independently and apart from the two activity groups discussed above, DLA Document Services is the preferred provider for document automation services to the DoD and is also designated as the single manager for printing and high-speed, high-volume duplicating in the DoD. Document Services provides printing, duplicating, and document automation services within the DoD to include document workflow conversion, electronic storage and output, multifunction devices, office printers, and distribution of hard copy and digital information. Through Document Services, DLA WCF helps customers reduce storage costs, increase efficiency of information sharing, and provide more functionality at a significantly lower cost.

**White House Display**

DLA's Document Services Data Production Lead, Mischelle O'Neal, working at a DLA print facility in the Eisenhower Executive Office building is mounting photos for framing and display around the White House Complex. **Photo by:** Nutan Chada, DLA Public Affairs

# General Fund

There are five major activities within DLA GF. DLA GF receives appropriations under the Agency identifier code for the OUSD (Treasury Index (TI)-97), along with Other Defense Organizations (ODOs). OUSD (Comptroller) (OUSD(C)) uses a data element referred to as a 'limit' to identify the various ODOs under TI-97. Defense-wide (DW) appropriations allotted to DLA GF include: (1) Operation and Maintenance (O&M), (2) Procurement Defense-wide (PDW), (3) Research, Development, Test and Evaluation (RDT&E), (4) Military Construction (MILCON), and (5) Family Housing O&M. The appropriations provide the funding to incur obligations and to pay for goods and services. DLA GF sub-allots RDT&E and MILCON funding to other DoD organizations (i.e., Defense Microelectronics Activity (DMEA), USACE and U.S. Naval Facilities Engineering Command (NAVFAC)). DLA GF is responsible for reporting sub-allottee balances in the DLA GF AFR.

## Operation and Maintenance (O&M)

O&M funds have an availability period of one year. DLA GF uses appropriations to support the sustainment of ongoing mission support initiatives at the Agency level and department wide. The O&M appropriation continues the path to achieving full spectrum readiness and advances DoD's multi-pronged, multi-year approach to build a more lethal and ready force with targeted investments in industrial readiness, microcircuit emulation, and soldier and family programs. For the years ended September 30, 2023, and 2022, O&M was appropriated a total of $419.6 million and $426.8 million, respectively.

## Procurement Defense – Wide (PDW)

PDW funds have an availability period of three years. As the Nation's Combat Logistics Support Agency, DLA procures, manages, stores, and distributes items that the components of the DoD (including the U.S. Army, Navy, and Air Force, Marine Corps and Space Force) need to operate. Commodities include everything from maritime and land weapons systems support to medical supplies. DoD uses the appropriations to obtain various categories of material, such as: new military hardware, aircraft, armored vehicles, and other major equipment; upgrades to existing equipment, including extending service life or remanufacturing existing systems; weapons and ammunition, ranging from air-to-air missiles to rounds for individual rifles; and spare parts, particularly those that are centrally managed. For the years ended September 30, 2023, and 2022, PDW was appropriated a total of $24.5 million and $510.9 million, respectively, for funding of equipment.

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

RDT&E funds have an availability period of two years. To maintain technological superiority on the battlefield, DoD relies on scientific and technical knowledge developed in large measure through RDT&E. DLA's RDT&E funding is appropriated in Title IV Research, Development, Test and Evaluation. DLA's Research & Development (R&D) is a program funded by the RDT&E appropriation that enables supply-chain innovation that directly supports the Warfighter. The program's goal is to deliver innovative and responsive solutions to the Warfighters and other valued customers. For the years ended September 30, 2023, and 2022, RDT&E was appropriated a total of $356.7 million and $350.0 million, respectively. DLA's RDT&E funds are primarily sub-allotted to DMEA for execution. Due to the long-term nature of research projects, DMEA funds are held by DLA GF and released to suballottees on a scheduled basis based on the project phase and related funding categories. From the FY 2023 newly appropriated funds, DMEA was sub-allotted a total of $207.3 million.

## Family Housing (O&M, Defense-Wide)

Family Housing funds have an availability period of one year. The Family Housing appropriations encompass Military Family Housing (MFH) authorized by law to meet the requirements of the DoD and include all DoD Component family housing, leases of real property utilized by DoD Components for family housing, and associated family housing support services. DLA GF did not receive Family Housing appropriations in FY 2023 as DLA GF has divested all its Family Housing units. Due to the size and materiality of Family Housing, DLA GF combined the Family Housing program with MILCON in its Statements of Net Cost for presentation and reporting purposes.

## Military Construction (MILCON)

MILCON funds have an availability period of five years. MILCON appropriations are provided to construction agents. The three main funding categories include: (1) planning and design for the initial engineering phase of developing and scoping of all MILCON projects; (2) major construction to replace or renovate DoD Fuels, Distribution, and Inventory Control Point Facilities around the world; and (3) unspecified minor construction to address lower dollar add-on/related smaller projects, which emerge as new requirements during the major construction process, and were not included in the original scope of the major construction projects. For the year ended September 30, 2023, and 2022, MILCON was appropriated a total of $220.5 million and $137.5 million, respectively. DLA's MILCON funds are primarily sub-allotted to USACE and NAVFAC for execution. Due to the long-term nature of construction projects, MILCON funds are held by DLA GF and released to suballottees on a scheduled basis based on the project phase and related funding categories. From the FY 2023 and FY 2022 newly appropriated funds, USACE was sub-allotted a total of $47.3 million and $10.0 million, respectively. From the FY 2023 newly appropriated funds, NAVFAC was sub-allotted a total of $446 thousand. No newly appropriated FY 2022 funding was sub-allotted to NAVFAC in FY 2022.

# National Defense Stockpile Transaction Fund

The DLA Strategic Materials (SM) program is a distinct revolving fund which operates under the authority of the Strategic and Critical Materials Stock Piling Act (50 U.S.C. §98, et seq.) (the Act). The mission of the National Defense Stockpile (NDS) program is to provide for the acquisition and retention of stocks of certain strategic and critical (S&C) materials, and to encourage the conservation and development of sources of S&C materials within the United States. The major activity within the DLA NDSTF is the acquisition and storage of S&C Materials as part of managing and operating the Nation's NDS. DLA SM strives to decrease and preclude a dangerous and costly dependency upon foreign sources or a single point of failure for supplies of such materials in times of National Emergency. DLA SM operational goals for the NDS include ensuring efficient and responsible resource stewardship and the highest environmental standards.

Along with providing operational oversight and acquisition and retention of stockpile materials, DLA SM provides for the conversion and upgrade of stockpile materials to prevent obsolescence, the recycling of strategic materials from end- of-life Government items and disposes of excess stocks through a public sales program. The Stockpile Sales Program provides operational funding for the NDS. DLA SM performs analyses, planning, procurement, and management of materials critical to National security. DLA SM serves clients through a unique combination of technical expertise, global/geopolitical S&C material supply analyses, management of existing critical materials, and broad range tracking of future critical materials.

The DLA SM revenues are generated through public sales offerings to pre-qualified customers of stocks determined excess to DoD needs. The Annual Materials Plan serves as notification to Congress of NDS material plans for a given fiscal year. The Annual Sales Plan (ASP) is the execution plan for disposals via the Stockpile Sales Program and designates inventory available for sale. Receipts collected represent the source of funding for operational expenditures and new material acquisitions. Other financing sources relate to that of appropriations received for the acquisition and retention of certain stockpile materials, and activities pursuant to the Strategic and Critical Material Stock Piling Act, (50 U.S.C. 98 et seq.).


**Joint Logistics Course**

Patrick Kelleher, the Defense Logistics Agency's executive director of operations and sustainment, addressed students at the Army's Joint Logistics Course at Fort Lee, Virginia, March 3, 2023. Kelleher talked about the future of logistics and DLA's capabilities during his 90-minute presentation.
**Photo by:** Nancy Benecki

# Organizational Chart

Below is DLA's organizational chart. Appendix A contains further explanation of the Staff Directors and Field Activity Commanders (J/D) Codes.


**Figure 2**: DLA Organizational Chart

# DLA Organizational Structure

**Office of the Secretary of Defense**

**Under Secretary of Defense**
(Acquisition and Sustainment)

**Assistant Secretary of Defense**
(Sustainment)

**Defense Logistics Agency**
Fort Belvoir, VA

**DLA Distribution**
New Cumberland, PA

Provides storage and distribution solutions/ management, transportation planning/management and logistics planning and contingency operations; operates a global network of distribution centers.

**DLA Disposition Services**
Battle Creek, MI

Disposes of excess property by reutilization, transfer and demilitarization; and conducts environmental disposal and reuse.

**DLA Aviation**
Richmond, VA

Provides parts for aviation weapons systems, flight safety equipment, maps, environmental products, industrial hardware, and industrial plant equipment.

**DLA Land and Maritime**
Columbus, OH

Provides repair parts for ground-based and Maritime weapons systems, small arms parts, fluid handling, consumable hardware, and electronic components.

**DLA Troop Support**
Philadelphia, PA

Provides food, textiles, construction material, medical supplies, and equipment, to include pharmaceuticals.

**DLA Energy**
Fort Belvoir, VA

Provides bulk fuel, alternative fuel/renewable energy, aerospace energy, fuel quality/ technical support, fuel card programs and installation energy services.

**DLA CENTCOM & SOCOM**
MacDill Air Force Base, FL

**DLA EUCOM & AFRICOM**
Stuttgart, Germany

**DLA INDOPACOM**
Joint Base Pearl Harbor-Hickam, HI

**Figure 3:** DLA Organizational Structure

# Performance Goals, Objectives, and Results

The DLA has established performance assessments of its programs for purposes of evaluating Agency performance and improvement, based on the GPRA Modernization Act of 2010. DoD produces an Annual Performance Report (APR) for all its components, and will include its FY 2023 APR with its FY 2025 Congressional Budget Justification. The APR is located at: https://dam.defense.gov/Publications/Annual-Performance-Plan-and-Performance-Report/

The Performance Goals, Objectives, and Results within this section are aligned to DLA's 2021-2026 Strategic Plan and provides a summary of DLA's five Lines of Effort (LOEs) and three Critical Capabilities (CCs). These goal-oriented objectives and forward-looking initiatives are designed to strengthen DLA's efforts in sustaining Warfighter readiness and the Nation's responsiveness as described:

**Lines of Effort:** Key strategic priority used to link multiple objectives that when combined achieve an operational or strategic outcome.

**Critical Capabilities:** Agency enablers which are essential to accomplishing DLA's strategic objectives and LOEs.

**Objectives:** Specific goals to be achieved and are the most important actions essential to LOEs and Critical Capabilities – the "how" of the strategy.

The key initiatives that have the Director's specific emphasis in DLA's Strategic Plan for 2021-2026 are shown in the LOEs and CCs below.

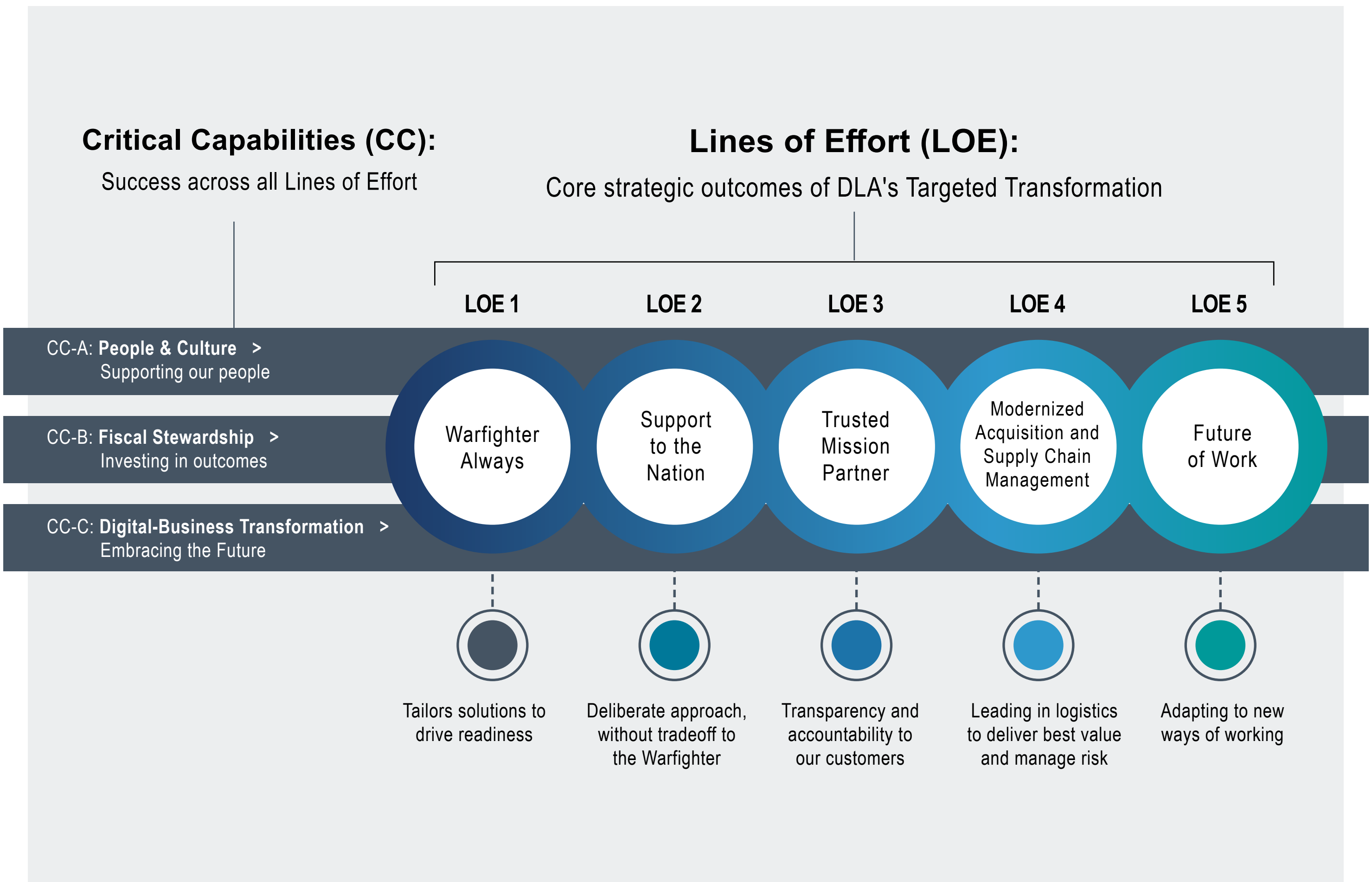



**Figure 4:** Lines of Effort and Critical Capabilities

*The LOEs, CCs and objectives in the section below are derived from DLA's 2021-2026 Strategic Plan; however, there are specific objectives and key performance measures that are applicable to DLA and have been identified accordingly below*

## LOE 1: Warfighter Always

**Objective 1.1:** Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments

**Objective 1.2:** Partner with customers at the wholesale and retail levels to address Service-specific challenges and develop solutions

**Objective 1.3:** Proactively support the DoD Nuclear Enterprise and Space Enterprise

DLA's support to the Warfighter is job one. It's our core strategic priority. We must provide the right support in the right places at the right times.

The Military Services and Combatant Commands have unique needs and capabilities requiring customized solutions.

It's imperative for DLA to make smart, disciplined investments in innovative tailored logistics solutions to increase and sustain weapons system and warfighting readiness – including our Nation's strategic deterrent – to meet today's requirements and prepare for the future fight.

## LOE 2: Support to the Nation

**Objective 2.1**: Implement a deliberate, enterprise-wide approach to Whole of Government support

Capitalizing on our scope, scale and skills in acquisition, storage, distribution, and surge capabilities, the Nation has increasingly called upon DLA to provide Whole of Government support.

DoD is redoubling its commitment to a cooperative, whole-of-nation approach to national security that builds consensus, drives creative solutions to crises, to guarantee that we lead from a position of strength.

As part of this effort, this LOE clarifies a deliberate approach to our Whole of Government mission with no cost trade-off to the Warfighter.

## LOE 3: Trusted Mission Partner

**Objective 3.1:** Implement customer-centric performance metrics and predictive problem-solving culture

**Objective 3.2:** Provide greater financial transparency to customers

**Objective 3.3:** Provide next generation customer service, including a customer feedback mechanism

Building trust begins with understanding our customers' priorities. Through a collaborative, data-driven problem-solving culture, we will pursue viable solutions to these critical challenges.

DLA will improve trust and transparency by enhancing customer-facing tools and software, formalizing customer feedback and increasing collaboration at all levels. We will align performance metrics and targets to ensure we are accountable to our customers.

## LOE 4: Modernize Acquisition and Supply Chain Management

**Objective 4.1:** Expand industry engagement to foster innovation and maximize value for our customers

**Objective 4.2:** Improve the end-to-end post-award segment to enable collaborative customer support, increase responsiveness, and manage costs

**Objective 4.3:** Develop a market intelligence capability to manage supply chain risk and drive best value

**Objective 4.4:** Enhance our acquisition capabilities to improve readiness for contingencies

The global logistics environment is rapidly evolving and increasingly interconnected. DLA must work closely with industry partners to modernize and streamline our acquisition and end-to-end supply chains to deliver increased readiness and maintain our competitive advantage.

Through strong partnerships with our suppliers, and an enhanced focus on market intelligence capabilities, DLA will continue building a diverse, resilient, and agile industrial base to reduce supply chain risk and drive the best value for our customers.

Given the increasing number of global contingencies, this will better position us and our partners to meet the accelerating challenges in an ever-changing world.

At the heart of this LOE is the ability to increasingly harness and analyze business performance data to make informed, risk-based decisions and develop actionable solutions to improve customer outcomes for routine and contingency operations.

**Photo by:** Burst on Unsplash

## LOE 5: Future of Work

**Objective 5.1:** Redefine virtual work models to enable our next generation workforce

**Objective 5.2:** Assess DLA CONUS facilities footprint to maximize space utilization

**Objective 5.3:** Build skillsets of the future

The workplace is increasingly virtual, reducing the need for a large physical footprint. Ongoing modernization efforts such as the use of mobile tablets, voice technology, autonomous guided vehicles and other advances to optimize warehouse operations all impact the future of work. DLA will continue adapting to these changes as it attracts and sustains a competitive workforce to drive increased productivity and employee satisfaction.

Creating an optimal work environment for employees that is modern, safe, secure, and well maintained will help increase retention and expand our access to diverse talent pools.

## DLA Critical Capabilities

The three Critical Capabilities are fundamental to our successful transformation. They intersect and support the five LOEs with specific underlying objectives, initiatives, and metrics.

- **CC-A:** People and Culture Supporting our people
- **CC-B:** Fiscal Stewardship Investing in outcomes
- **CC-C:** Digital-Business Transformation Embracing the future

### Construction Crew

Navy Petty Officer 2nd Class Ian Potter works with a soldier assigned to the Georgian Land Force's 2nd Brigade Engineering Company to vibrate and strengthen a concrete pad for a railhead project in Poti, Georgia, Dec.15, 2022. **Photo By:** Navy Builder Constructionman Gabriella Coupe

In these areas, DLA must be ready to act, adapt, reform, and embrace change to improve our organizational efficiency and effectiveness.

## Critical Capability A: People and Culture

**Objective A1:** People

**Objective A2:** Culture

Our most important asset as an Agency is our people. This capability aligns DLA's proven human capital strategies with our mission, LOEs, and objectives.

Our ability to attract, develop, and retain a diverse, skilled, and agile workforce is vital to our continued success.

To achieve a shared vision with the Agency's Strategic Plan, all DLA organizations, employees and leaders must work together to fortify the culture, reward high performance, build connections, and prioritize safety of the workforce.

## Critical Capability B: Fiscal Stewardship

**Objective B1:** Auditability

**Objective B2:** Cost visibility and cash management

**Objective B3:** Investment to drive efficiency and effectiveness

In an increasingly resource-constrained environment we will drive cost effectiveness while maintaining Service readiness. We must effectively manage our resources while making smart, transformative investments that increase value for our customers and taxpayers.

Through enhanced tools and capabilities, we will improve our cost and cash management for the DLA Working Capital Fund.

We will assess our work processes and the effectiveness of current internal controls to provide greater transparency, improve auditability and prevent fraud, waste, and abuse.

## Critical Capability C: Digital Business Transformation

**Objective C1:** Transformational information technology capabilities

**Objective C2:** Advanced analytics and automation

**Objective C3:** Cybersecurity

**Objective C4:** Technology governance

Technology is changing at an exponential rate, generating new possibilities in logistics and customer support. It is also increasing the capabilities of our competitors, the risks to our supply chains and operations.

We are focusing our Information Technology (IT) and digital capability investments on key areas that will enable us to enhance performance, reduce costs, and make more predictive and data-driven decisions.

We will transform our systems and processes to improve transparency, reliability, and security for our employees, customers, and suppliers.

**Pallet Partners**
Sailors move supplies on the flight deck of the USS Leyte Gulf during a replenishment in the Ionian Sea, Jan. 28, 2023. **Photo by:** Navy Petty Officer 2nd Class Christine Montgomery

# Performance Measures (Unaudited)

## DLA Performance Measure: Future of Work

This performance measure relates to the objectives described above:

***Objective 5.1:*** *Redefine virtual work models to enable our next generation workforce;* ***Objective 5.2:*** *Assess DLA Contiguous United States (CONUS) facilities footprint to maximize space utilization; and* ***Objective 5.3:*** *Build skillsets of the future*

The DLA Human Resources (HR) is tasked with advancing a co-operative and supportive workplace culture. That culture was instrumental in allowing the Department to quickly adapt to extensive telework for many employees in the early days of the pandemic, while also allowing the Department to meet mission requirements under the unprecedented conditions.

The U.S. Office of Personnel Management (OPM) conducted annual employee surveys for DLA for years 2019 through 2022. From 2019 (pre-pandemic) to 2020, the surveys indicated that department-wide teleworking three or more days a week increased approximately 270.5% and overall employee satisfaction with the DLA organization increased by 11.5%. For the years 2020 through 2022, teleworking three or more days a week decreased 18.0% while overall employee satisfaction with the DLA organization decreased 11.1%.

As the employee survey is conducted annually during October/November, the FY 2022 data is the latest available for the FY 2023 AFR.

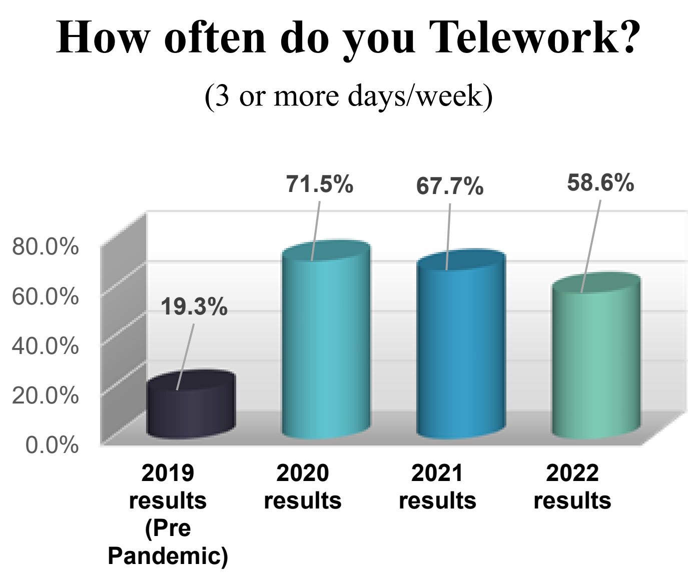



**Figure 5:** How often do you telework?


**Figure 6:** Has DLA provided increased opportunities for Telework?

Based on this data, it is expected that continuing the increased virtual work environment after COVID will support attracting and sustaining a competitive workforce, increased productivity, and heightened employee satisfaction.

DLA HR is addressing the dynamics of employee satisfaction as part of its focus on the “ever changing work force”. DLA HR continues to assess existing resource initiatives and to develop new strategies to excel in areas such as recruitment, training and development, work-life balance, managing in a geographically dispersed environment while maintaining strong connections to DLA culture, knowledge transfer, leadership skills, labor management relations and a culture that fosters diversity, equity, inclusion, accessibility, and employee engagement.

## **Performance Measure:** DLA Roadmap to Auditability

This performance measure relates to the objective described above:

***Objective B1:*** *Auditability*

Currently, DLA WCF, GF, and NDSTF receive disclaimers of opinion on its financial statements. DLA WCF, GF, and NDSTF are striving to obtain unmodified audit opinions from its IPA in the future. Since receiving a disclaimer of opinion each year from FY 2017, DLA has taken a two track approach in resolving major impediments in efforts to strive for an unmodified audit opinion: (1) improving the reliability and fair presentation of financial data reported in the AFR by identifying root causes of conditions, prioritizing resources, and developing action plans to address Notice of Findings and Recommendations (NFRs); and (2) developing, improving, and refining the underlying end- to-end processes that support the compilation of the AFR by instilling sound fundamental practices in accordance with U.S. GAAP. The following timeline summarizes the occurrence of events that propelled DLA into a corrective action posture.

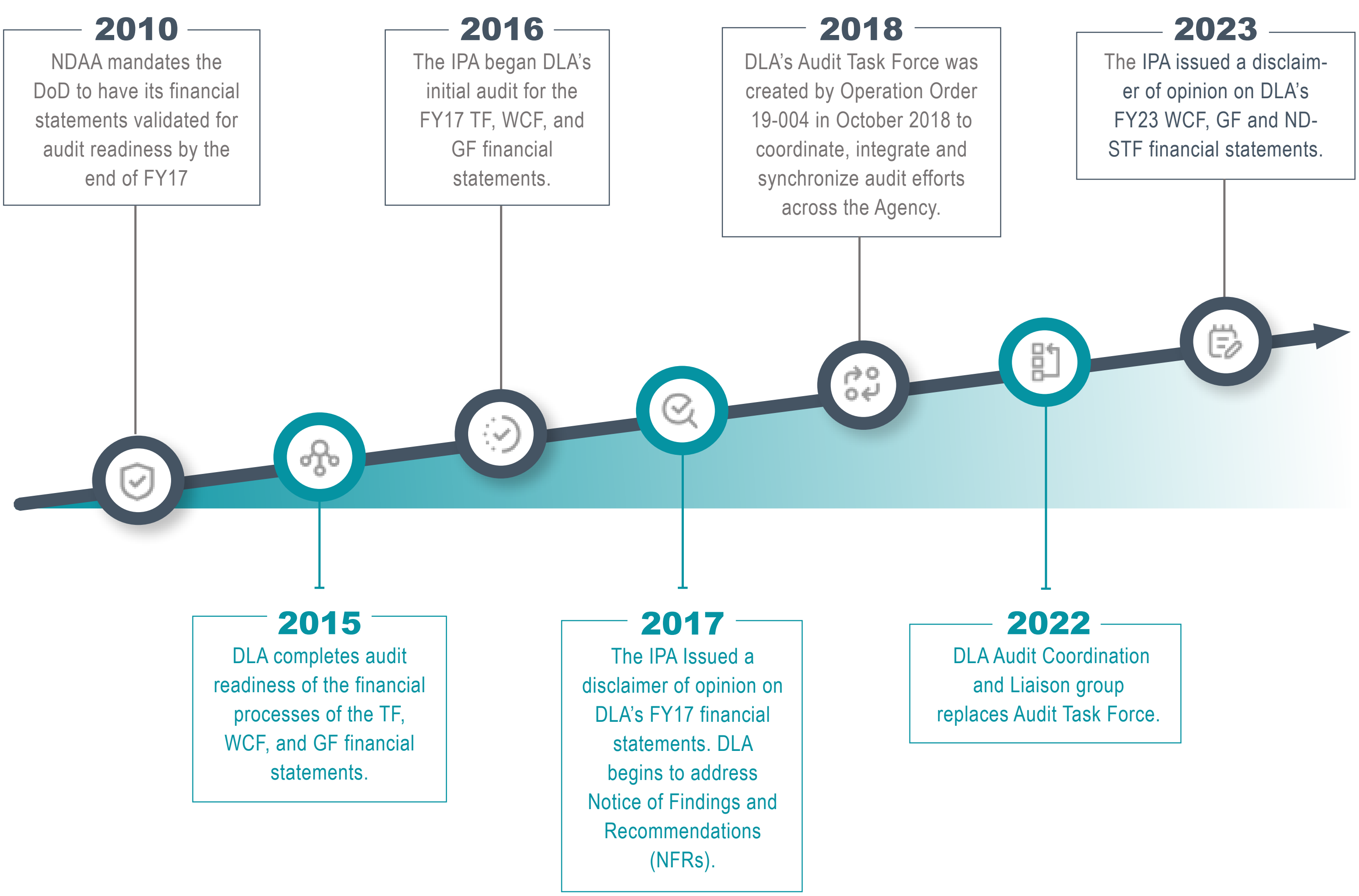
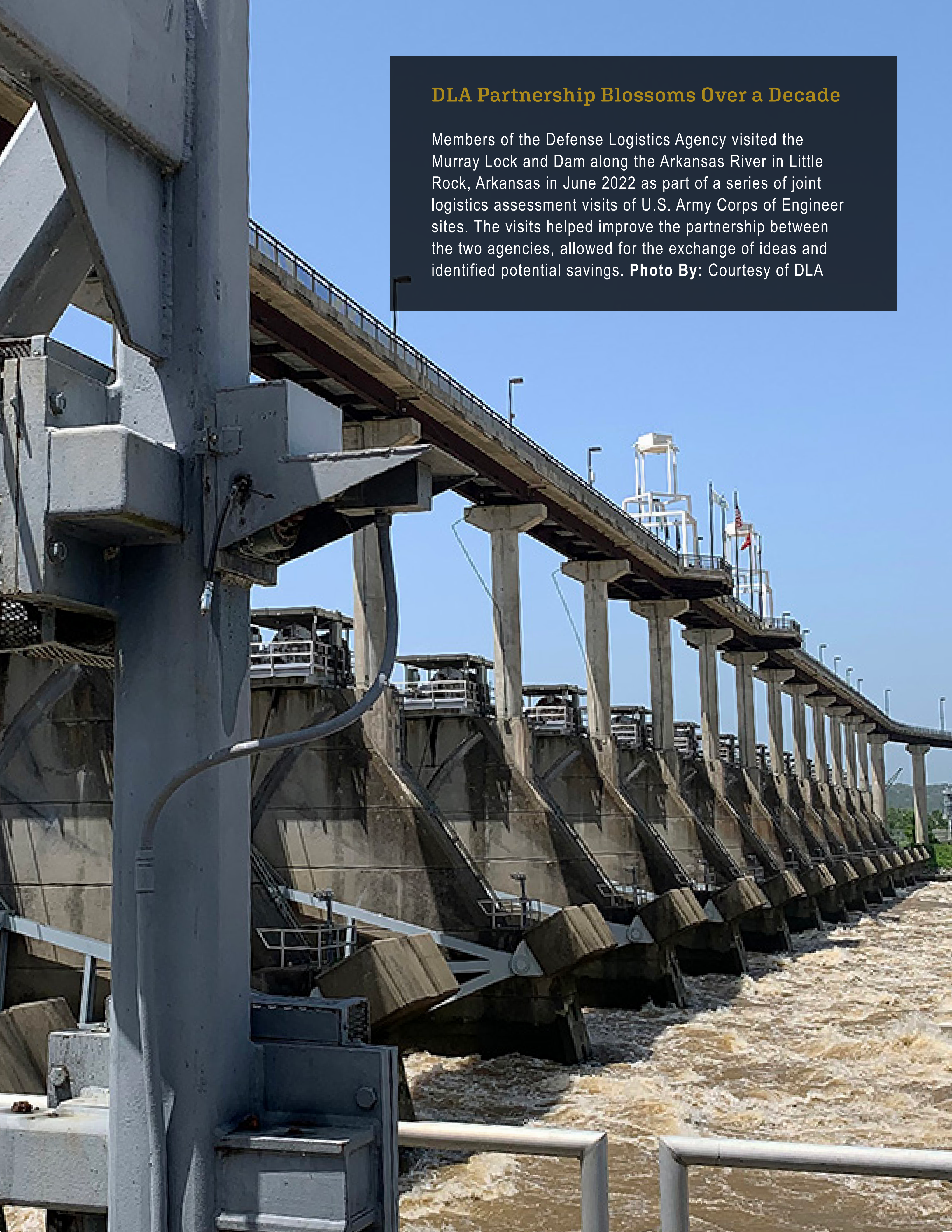



**Figure 7:** DLA Auditability Timeline



## DLA Partnership Blossoms Over a Decade

Members of the Defense Logistics Agency visited the Murray Lock and Dam along the Arkansas River in Little Rock, Arkansas in June 2022 as part of a series of joint logistics assessment visits of U.S. Army Corps of Engineer sites. The visits helped improve the partnership between the two agencies, allowed for the exchange of ideas and identified potential savings. **Photo By:** Courtesy of DLA

# Working Capital Fund

## DLA WCF Performance Measure 1:
SCM Supply Availability to Warfighters

This performance measure relates to the objectives described above

***Objective 1.1:*** *Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments; and* ***Objective 4.4:*** *Enhance our acquisition capabilities to improve readiness for contingencies*

The DLA SCM strives to predict supply needs to equip the Warfighter efficiently and effectively. The following analysis applies to Non-Mission Capable Supply; the results display acquisition and supply activities for regular procurement items. DLA continues its efforts in meeting high supply availability expectations by employing smart budgetary resource use techniques and leveraging rapid acquisition opportunities to meet expectations. WCF Supply Chain Management will continue to evaluate purchases, storage, and distribution processes, and plans to implement cost-justified modifications to increase efficiency and supply availability in future periods.

Supply Availability's targeted expectation range, per OSD requirements, is 82% to 89%, providing an aggregate target of 85%. In FY 2023, Non-Mission Capable Supply Availability has performed within this given range, but two of the four services are below the 85% goal. The degradation in FY 2022 and FY 2023 performance is the result of a targeted restriction in funding due to DLA's overstated demand projections in previous fiscal years. During FY 2020, DLA began to realize that expenses started to outpace income. Measures were taken to balance the cash flow, namely, a reduction in procurements to cut costs. This resulted in a reduction of inventory, leading to a decrease in Supply Availability. In addition to these budgetary restrictions, the COVID pandemic disrupted DLA's supplier base, leading to longer fulfillment lead times. DLA operations have been refining the data accumulation and reporting for this measurement, and prior year amounts currently being reported reflect improved data accumulation and categorization.

For the year ended September 30, 2023, WCF SCM Supply Availability presentation changed from prior year to more closely align with current program goals and activity. Medical and Subsistence supply chains have been removed from presentation due to the nature of their business. In relation to the other supply chains, Medical and Subsistence have a much smaller percentage of backorders and backorder resolution that is not a core measurement of their business processes. This reflects a more comparable presentation of supply chain data to assess current performance.


**Idaho Lands receives donated equipment from DLA**

South Boundary Rural Fire District Type 4 Wildland Engine formerly served as an Army M1083A1 before donation by Defense Logistics Agency Disposition Services to the Idaho Department of Public Lands. The vehicle is part of the $70 million in used and surplus equipment the Idaho department has received from DoD since 2013. **Photo by:** Idaho Dept. of Lands

# Supply Availability to Warfighters

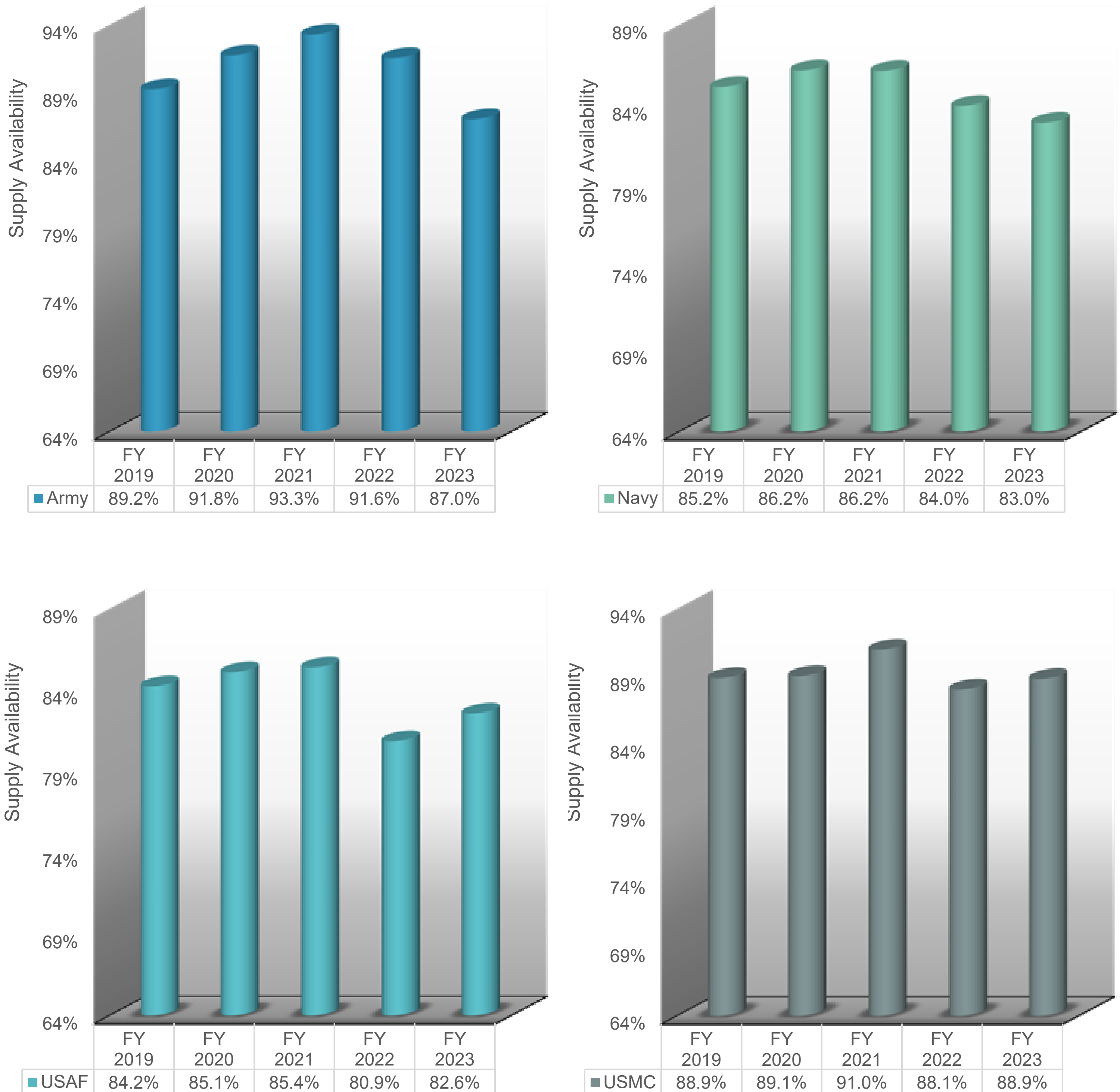



**Figure 8:** Supply Availability to Warfighters by Military Command

## DLA WCF Performance Measure 2:
## SCM "Wait Time" to Fill Supply Orders for Supply Chains

This performance measure relates to the objectives described above

***Objective 1.1:*** *Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments; and* ***Objective 4.4:*** *Enhance our acquisition capabilities to improve readiness for contingencies*

The DLA WCF tracks the average amount of wait time that occurs to fill backorders for its SCM. DLA WCF aims to minimize the amount of time required to fill backorders to increase the readiness of the Warfighter. DLA WCF's emphasis on filling high priority non-mission capable supply backorders and weapon system readiness-based orders has allowed lower priority orders to age more than in the past. When those lower priority orders are not filled, they drive up the average wait time. In recent fiscal years, DLA has implemented restrictions on stock replenishment for inventory budgeting purposes. While SCM sales have continued to meet program goals, the reduced inventory funding has resulted in less inventory in-stock and less inventory on order with DLA vendor's, ultimately driving-up backorder resolution time. Additionally, FY 2021 and FY 2022 supply chain disruptions were driven by the COVID-19 Pandemic, also having an unfavorable impact on wait time.

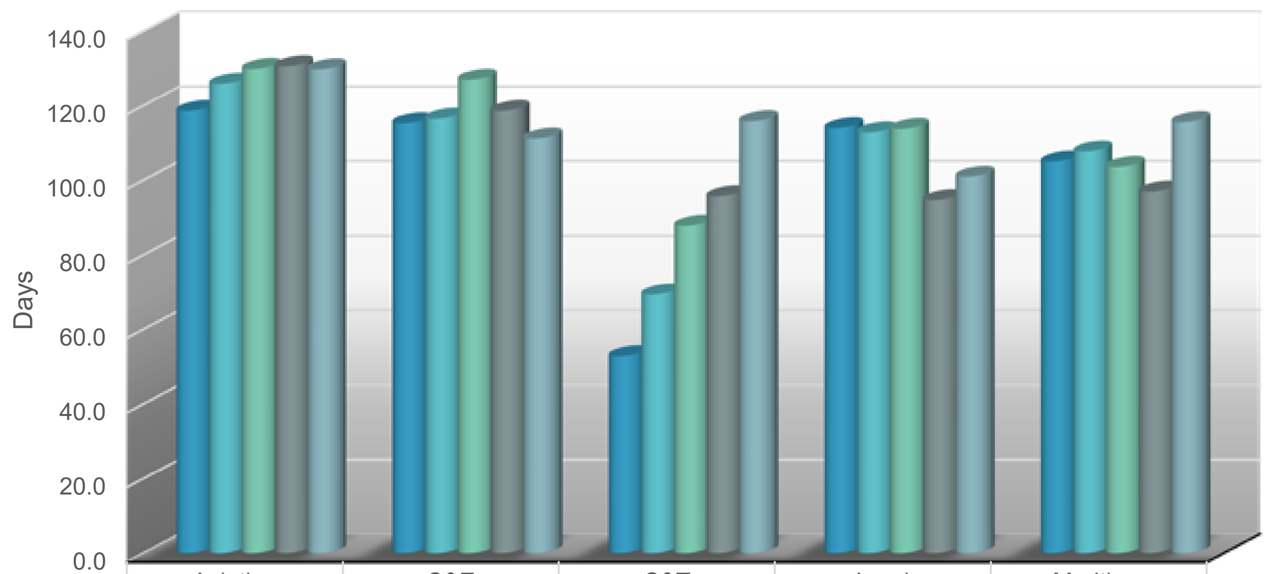
The DLA SCM wait time to fill backorders for the Military Departments over the past five fiscal years is illustrated below for the following SCM supply chains: Aviation, Land, Maritime, C&E, and C&T. The IH supply chain, which had existed in prior years, was realigned in FY 2022, with its activity transferred to DLA Aviation and DLA Land and Maritime. This realignment is expected to create future efficiencies and support increased material volume.

DLA WCF SCM applies variable strategic acquisition techniques to minimize supply wait times to supply the Warfighters efficiently and effectively WCF Supply Chain Management will continue to evaluate supply purchases, storage, and distribution processes, and plans to implement cost-justified modifications to increase efficiency and supply availability in future periods. DLA operations have been refining the data accumulation and reporting for this measurement, and prior year amounts currently being reported reflect improved data accumulation and categorization.

For the year ended September 30, 2023, WCF SCM wait time to fill presentation changed from prior year to more closely align with current program goals and activity. Medical and Subsistence supply chains have been removed from presentation due to the nature of their business. In relation to the other supply chains, Medical and Subsistence have a much smaller percentage of backorders and backorder resolution that is not a core measurement of their business processes. This reflects a more comparable presentation of supply chain data to assess current performance.

**DLA Distribution Installation Management**
A rendered image of the future for Defense Logistics Agency Distribution Red River, Texas. The solar output from the proposed project is anticipated to generate over 1200 megawatts annually. **Photo by:** Courtesy of DLA

# Wait Time to Fill Backorders for Supply Chain Management




| | Aviation | C&E | C&T | Land | Maritime |
|---|---|---|---|---|---|
| FY 2019 | 118.6 | 115.3 | 52.9 | 114.0 | 105.0 |
| FY 2020 | 125.9 | 116.5 | 69.4 | 112.9 | 107.7 |
| FY 2021 | 129.9 | 127.0 | 87.9 | 113.8 | 103.6 |
| FY 2022 | 130.6 | 118.6 | 95.7 | 94.7 | 97.0 |
| FY 2023 | 129.8 | 111.2 | 115.8 | 101.0 | 115.6 |

**Figure 9:** Wait Time to Fill Supply Orders for Supply Chain Management (in days)

### Globemaster Support

Urban Search and Rescue members from Fairfax County, Va., sit aboard a C-17 Globemaster III at Dover Air Force Base, Del., Feb. 7, 2023, as the base supports earthquake response efforts in Turkey. The U.S. Agency for International Development is mobilizing emergency humanitarian assistance following the worst earthquake to hit the region in nearly a century. **Photo by:** Air Force Senior Airman Faith Barron

## DLA WCF Performance Measure 3:
## SCM "COVID-19 Support"

This performance measure relates to the objective described above

***Objective 2.1:*** *Implement a deliberate, enterprise-wide approach to Whole of Government support*

The DLA provides agency-wide pandemic support to aid the whole-of-government COVID-19 response, which became apparent in February 2020. For instance, DLA Disposition Service provides reutilized medical supplies, while DLA Land and Maritime provides repair parts for hospital ships, and DLA Energy provides the fuel.

The DLA WCF, in partnership with HHS, FEMA and other Federal Agencies, works to support the president in responding to COVID-19 challenges in procuring personal protective equipment (PPE) and replenishing the nearly depleted Strategic National Stockpile (SNS). DLA Troop Support is primary in this effort, coordinating procurement and delivery activities for COVID-19 supplies and SNS replenishment. The supplies procured as of September 30, 2023, as illustrated below, include test components, gloves, hand sanitizers, masks, N95 respirators, gowns, BinaxNOW POCs, COVID-19 OTC self/home tests and COVID-19 test kits.

For the year ended September 30, 2023, DLA Troop Support's procurement goal based on customer orders was to supply 0.4 million test components, 162.6 million gloves, 0.2 million hand sanitizers, 11.8 million masks, 0.6 million N95 respirators, 2.2 million gowns, 0.2 million BinaxNOW POCs, 0.5 million COVID-19 OTC self/home tests, and 0.3 million COVID-19 test kits. COVID supply orders continue to decline due to diminished nationwide prioritized COVID actions. Furthermore, DLA expected COVID PPE supply orders to continue the trending decline into FY 2024, as the Coronavirus national and public health emergency expired May 11, 2023.

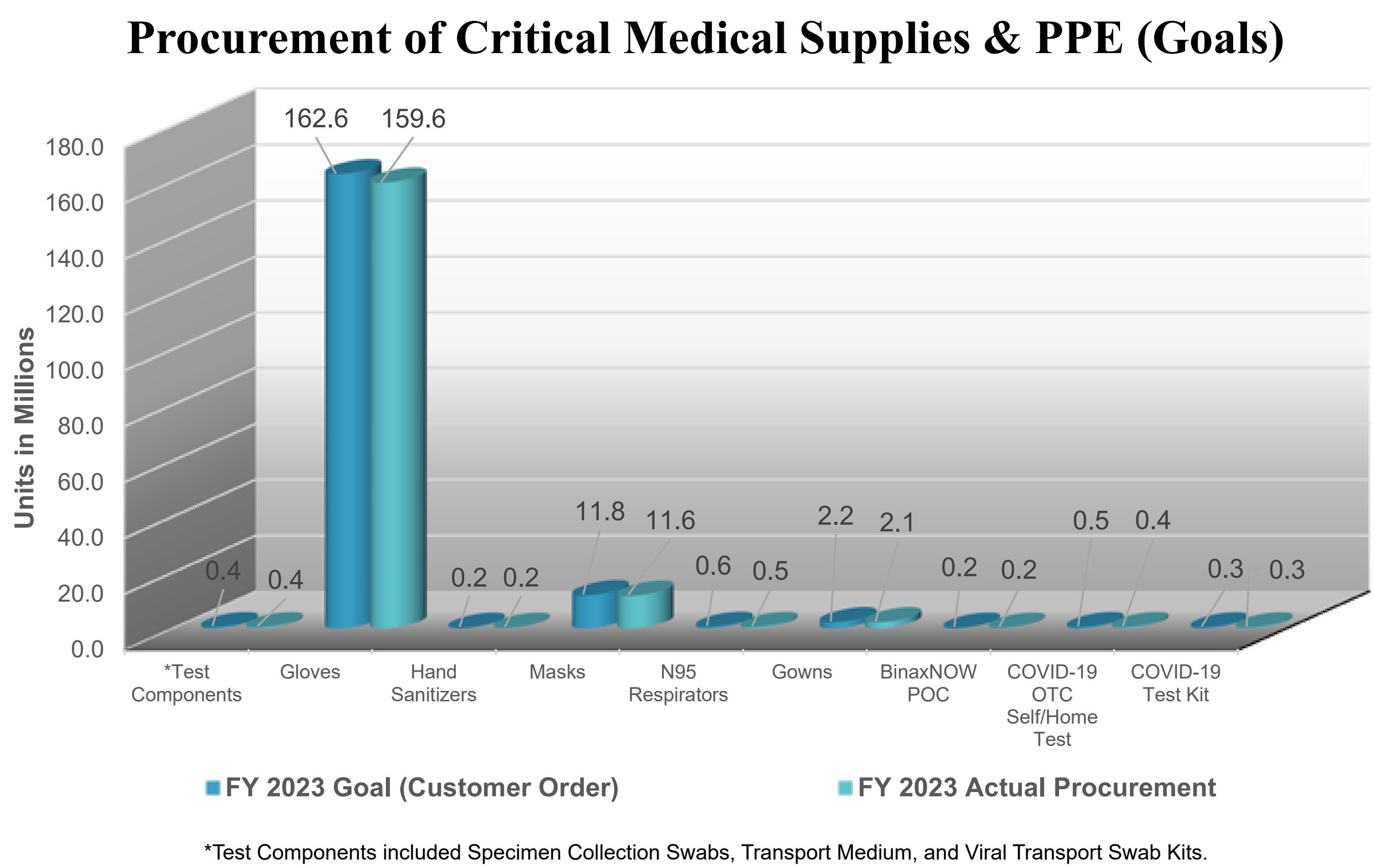
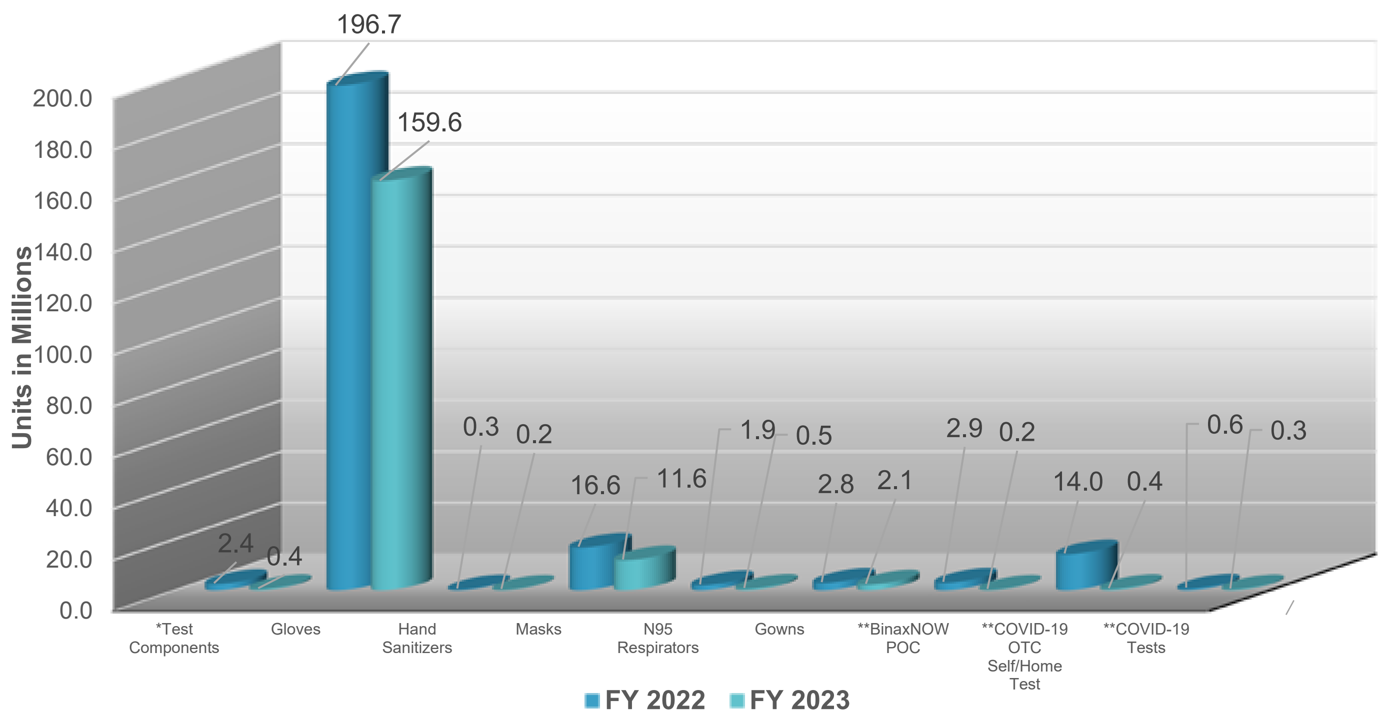



**Figure 10:** FY 2023 Procurement of Critical Medical Supplies & PPE versus Goal

## Procurement of Critical Medical Supplies & PPE




*Test Components included Specimen Collection Swabs, Transport Medium, and Viral Transport Kits
**BinaxNOW POC and COVID-19 OTC Self/Home Test are new supply categories added to the program in FY 2022

**Figure 11:** FY 2023 Procurement of Critical Medical Supplies & PPE versus FY 2022

### MRAP Training

Soldiers assigned to the Task Force Orion, 27th Infantry Brigade Combat Team, New York Army National Guard, conduct driver training and maintenance checks on mine-resistant ambush-protected vehicles in Grafenwoehr, Germany, Nov. 6, 2022. Task Force Orion is deployed to Germany in support of the Joint Multinational Training Group – Ukraine mission. **Photo by:** Army Staff Sgt. Jordan Sivayavirojna, New York National Guard

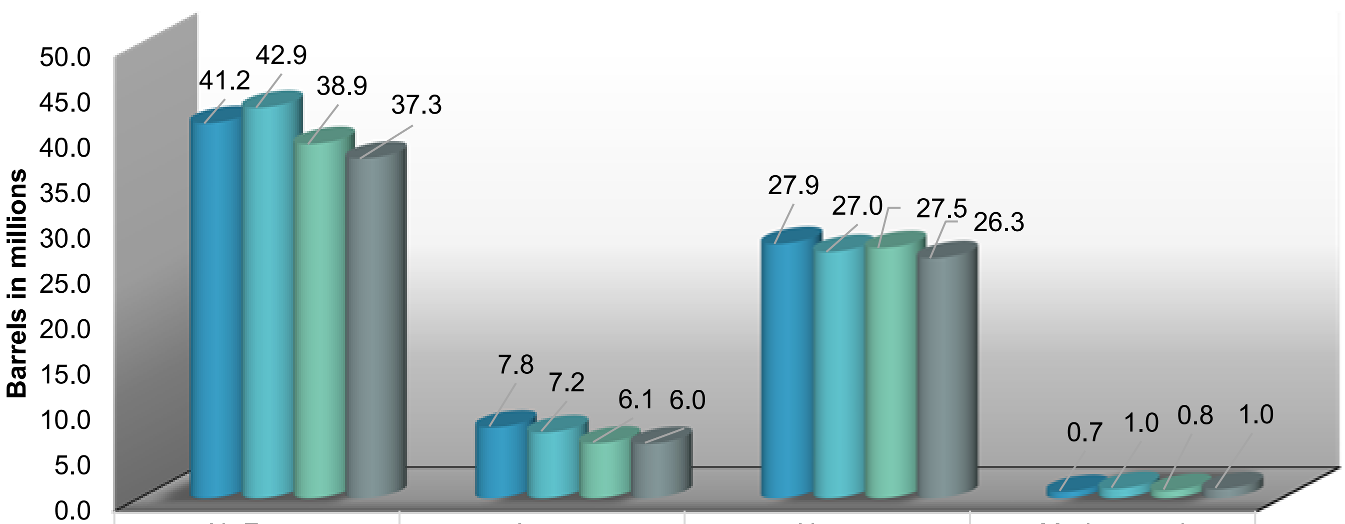
## DLA WCF Performance Measure 4:
## Energy Fuel Sales in Barrels by DoD Component

This performance measure relates to the objectives described above

***Objective 1.1:*** *Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments;* ***Objective 1.2:*** *Partner with customers at the wholesale and retail levels to address Service-specific challenges and develop solutions; and* ***Objective 2.1:*** *Implement a deliberate, enterprise-wide approach to Whole of Government support*

The DLA WCF supports other DoD Agencies through fuel sales. This allows for increased interagency support through self-sustainment of fuel. As of September 30, 2023, DLA Energy budgeted to sell 70.9 million barrels to DoD Agencies, and actual fuel sales to DoD components were 70.6 million barrels. DLA Energy actual fuel sales were 99.6% of budget and is considered to meet the budgeted goal for the performance year. Demand affects actual fuel sales year-over-year, and DoD's mission dictates the amount of fuel DoD purchases. For example, if training or flying hours decreased for DoD components, less fuel would be purchased during the year. WCF Energy will continue to evaluate fuel purchase, storage, and distribution processes, and plans to implement cost-justified modifications to increase efficiency and fuel availability in future periods.

### Fuel Sales in Barrels by DoD Component




| | Air Force | Army | Navy | Marines and Other DoD |
|---|---|---|---|---|
| FY 2020 | 41.2 | 7.8 | 27.9 | 0.7 |
| FY 2021 | 42.9 | 7.2 | 27.0 | 1.0 |
| FY 2022 | 38.9 | 6.1 | 27.5 | 0.8 |
| FY 2023 | 37.3 | 6.0 | 26.3 | 1.0 |

**Figure 12:** Fuel Sales in Barrels by DoD Component

## DLA WCF Performance Measure 5:
## Energy Fuel Sales in Dollars by DoD Component

This performance measure relates to the objectives described above

***Objective 1.1:*** *Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments;* ***Objective 1.2:*** *Partner with customers at the wholesale and retail levels to address Service-specific challenges and develop solutions; and* ***Objective 2.1:*** *Implement a deliberate, enterprise-wide approach to Whole of Government support*

As of September 30, 2023, DLA Energy budgeted to sell $11.8 billion of fuel to DoD Agencies, and actual fuel sales to DoD components were $11.8 billion. DLA Energy reports revenues on a net basis (gross revenues less direct cost).

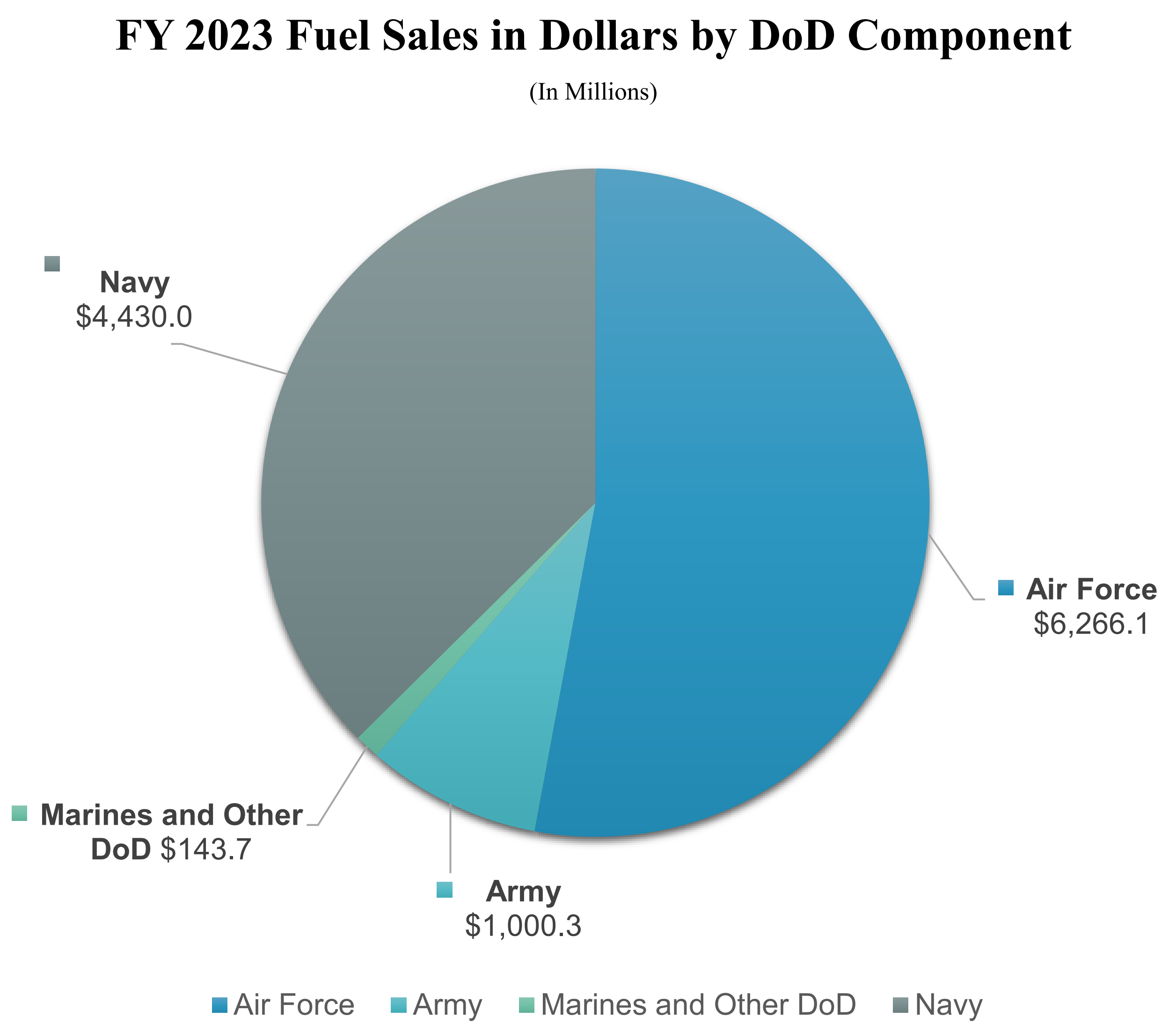



**Figure 13:** Fuel Sales in Dollars by DoD Component

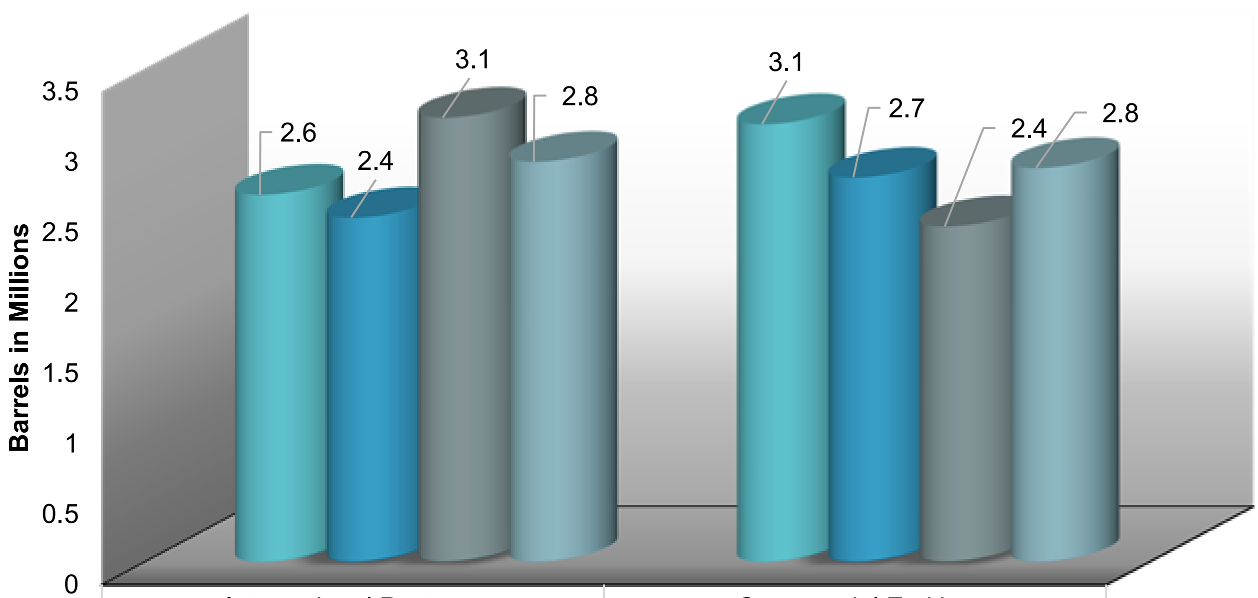
## DLA WCF Performance Measure 6:
## Energy Fuel Sales in Barrels by Non-Federal Customer

This performance measure relates to the objectives described above

***Objective 1.1:*** *Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments;* ***Objective 1.2:*** *Partner with customers at the wholesale and retail levels to address Service-specific challenges and develop solutions; and* ***Objective 2.1:*** *Implement a deliberate, enterprise-wide approach to Whole of Government*

The DLA is authorized to provide its services to the public by selling fuel to various non-Federal parties. By doing so, DLA is building partnerships with non-Federal customers, as well as international partners. As of September 30, 2023, DLA Energy budgeted to sell 7.0 million barrels to non-Federal customers, and actual fuel sales to non-Federal customers were 5.6 million barrels. Due to the reduction of operations overseas, the actual sales did not meet the budgeted sales for the period. WCF Energy will continue to evaluate fuel purchase, storage, and distribution processes, and plans to implement cost-justified modifications to increase efficiency and fuel availability in future periods.

**Fuel Sales in Barrels by Non-Federal Customer**




| | International Partners | Commercial Entities |
|---|---|---|
| FY 2020 | 2.6 | 3.1 |
| FY 2021 | 2.4 | 2.7 |
| FY 2022 | 3.1 | 2.4 |
| FY 2023 | 2.8 | 2.8 |

**Figure 14:** Fuel Sales in Barrels by Non-Federal Customers

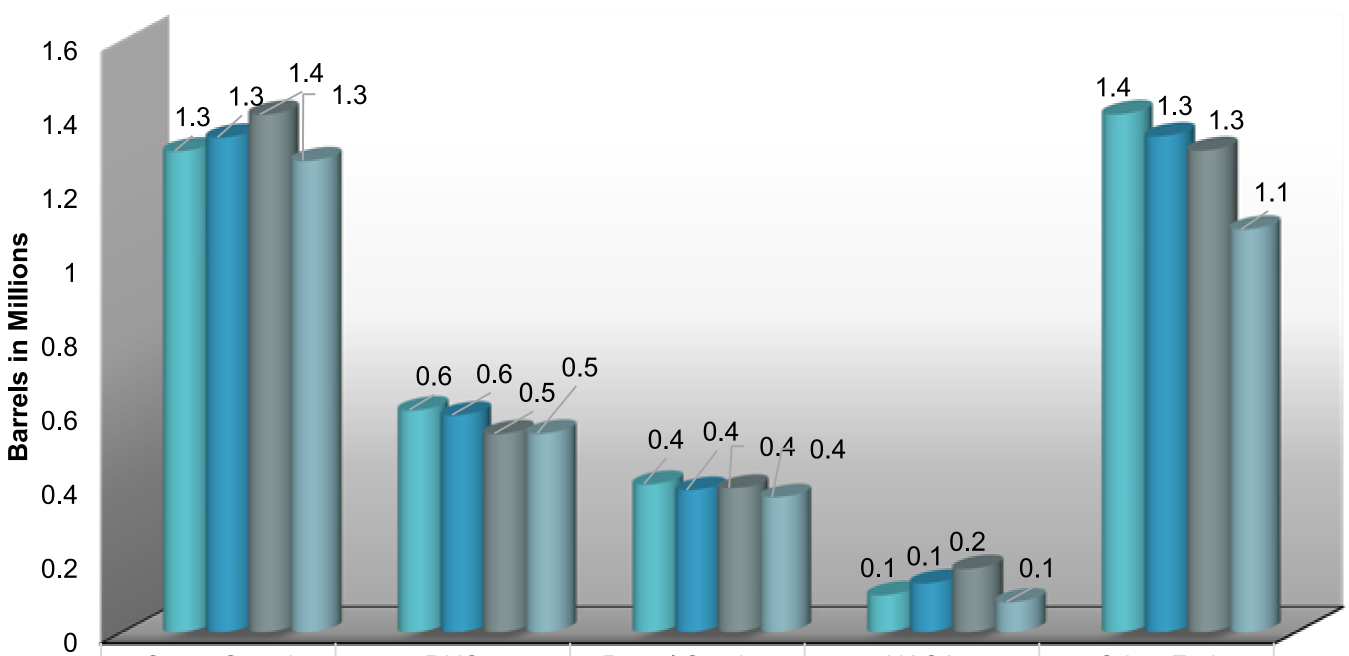
## DLA WCF Performance Measure 7:
### Energy Fuel Sales in Barrels by Federal Civilian Agency

This performance measure relates to the objectives described above

***Objective 1.1:** Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments; **Objective 1.2:** Partner with customers at the wholesale and retail levels to address Service-specific challenges and develop solutions; and **Objective 2.1:** Implement a deliberate, enterprise-wide approach to Whole of Government*

In addition to providing fuel to DoD components and non-Federal entities, DLA WCF also sells fuel to Federal Civilian Agencies. DLA WCF supports other Federal Agencies as they embark on their daily activities and accomplish their missions. DLA wholly supports the government and the entire Nation through its supply of fuel. As of September 30, 2023, DLA Energy budgeted to sell 4.2 million barrels to Federal Civilian Agencies. Actual fuel sales to Federal Civilian Agencies were 3.4 million barrels. The difference between actual and budgeted DLA Energy Fuel Sales by Federal Civilian Agencies represents less than 1% of total Energy sales, and is considered to meet the budgeted goal for the performance year. WCF Energy will continue to evaluate fuel purchase, storage, and distribution processes, and plans to implement cost-justified modifications to increase efficiency and fuel availability in future periods.

## Fuel Sales in Barrels by Federal Civilian Agency




| | Coast Guard | DHS | Postal Service | NASA | Other Fed Agencies |
|---|---|---|---|---|---|
| FY 2020 | 1.3 | 0.6 | 0.4 | 0.1 | 1.4 |
| FY 2021 | 1.3 | 0.6 | 0.4 | 0.1 | 1.3 |
| FY 2022 | 1.4 | 0.5 | 0.4 | 0.2 | 1.3 |
| FY 2023 | 1.3 | 0.5 | 0.4 | 0.1 | 1.1 |

**Figure 15:** Fuel Sales in Barrels by Civilian Agency

# General Fund

## DLA GF Performance Measure 1:
O&M Warstopper Program

This performance measure relates to the objectives described above

***Objective 1.3:*** *Proactively support the DoD Nuclear Enterprise and Space Enterprise;*
***Objective 2.1:*** *Implement a deliberate, enterprise-wide approach to Whole of Government support;*
***Objective 4.1:*** *Expand industry engagement to foster innovation and maximize value for our customers;*
***Objective 4.3:*** *Develop a market intelligence capability to manage supply chain risk and drive best value;*
*and* ***Objective 4.4:*** *Enhance our acquisition capabilities to improve readiness for contingencies*

### Readiness Investments

Readiness Investments in industry are made when the forecasted readiness demand is higher than the commercial industry is willing to invest. These types of investments can occur across all DLA Supply Chains including the DoD Nuclear Enterprise items. Additionally, DoD policy allows these industrial base measures to be used to offset War Reserve Material stocks and potentially avoid stock spoilage due to shelf-life expiration and changes to system configurations.

Warstopper investments are like a catastrophe or disaster business insurance policy and deliver expedited products to our customers (i.e., Military Services and Agencies) when triggered by an event (e.g., war, contingency, National Emergency, or disaster). Readiness investments support Objectives 1.3, 4.1, 4.3 and 4.4 by collecting market intelligence type information to confirm industrial base risk(s) exist, foster industry innovation to resolve industrial base risk, mitigate customer contingency requirement shortfalls and enhances acquisition alternatives to effectively and efficiently improve readiness for contingencies.

Another type of investment establishes a sub-tier raw material buffer. Buffers are established when there is a first-tier readiness issue caused by a raw material production input and the material is used by more than one producer. They are established with sub-tier suppliers to ensure the material title, certifications, pedigree, and warranty are passed on to the first-tier producer (e.g., manufacturer) or sub-tier component manufacturer. Material from these buffers can be directed towards many requirements including the DoD Nuclear Enterprise. The buffer material is not Government Furnished Material and the investment required is lower in cost then an end item investment and can have very wide application across the Defense Industrial Base (DIB). Performance is measured by the value of the finished mill material released from the buffer.

### Risk Analysis

Risk analysis and studies are used to determine the health of selected industries, as well as maintaining DLA industrial acquisition policies, assessing supplier on their ability to address surge and sustainment to meet readiness demand, and other program administrative duties.

The risk analysis program enables the DoD to be prepared, in the event of a potential threat to the security of the U.S., to take actions necessary to ensure the availability of adequate industrial resources and production capability, including services and critical technology for National defense requirements. These risk analyses and studies are an enabler for Objectives 1.3, 2.1, 4.1 and 4.4 by providing information to the appropriate decision makers and shared with other government agencies as appropriate.

Level-1 Risk Assessment (RA) is used to determine and verify if an industrial base issue exists or not, and Level-2 RA (i.e., study) is used to assess the risk and identify any industry potential risk mitigation strategies (e.g., acquisition strategies, Warstopper investments). A Level-1 RA is typically less than three months and a Level-2 RA is greater than three months to complete.

## DLA GF Performance Measure 2:
## O&M and RDT&E Defense Agencies Initiative Program

This performance measure relates to the objectives described above

***Objective 1.1:*** *Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments;* ***Objective 2.1:*** *Implement a deliberate, enterprise-wide approach to Whole of Government support; and* ***Objective 3.2:*** *Provide greater financial transparency to customers*

The Defense Agencies Initiative (DAI) is a financial management system of nine integrated business processes as displayed in Figure 16 below. The system provides real time, web-based accessible capabilities for financial managers and other DoD employees to make sound business decisions in support of the Warfighter. Currently, 29 Defense Organizations use DAI, including Defense Contract Audit Agency (DCAA), Defense Information Services Agency (DISA), United States Marine Corps (USMC), Missile Defense Agency (MDA), Defense Finance and Accounting Service (DFAS) and Naval Special Warfare (NSW). The DAI program continually requires innovation to meet the current dynamic technological and operational environment. As a result, in addition to O&M funding, the program also receives allotments through DLA GF RDT&E appropriations. In FY 2023, DAI was allotted $83.3 million of O&M funds, which represents 19.7% of DLA's total O&M appropriation of $422.0 million. In FY 2023, DAI was allotted $27.1 million of RDT&E funds, which is 7.6% of DLA's total RDT&E appropriation of $356.7 million.

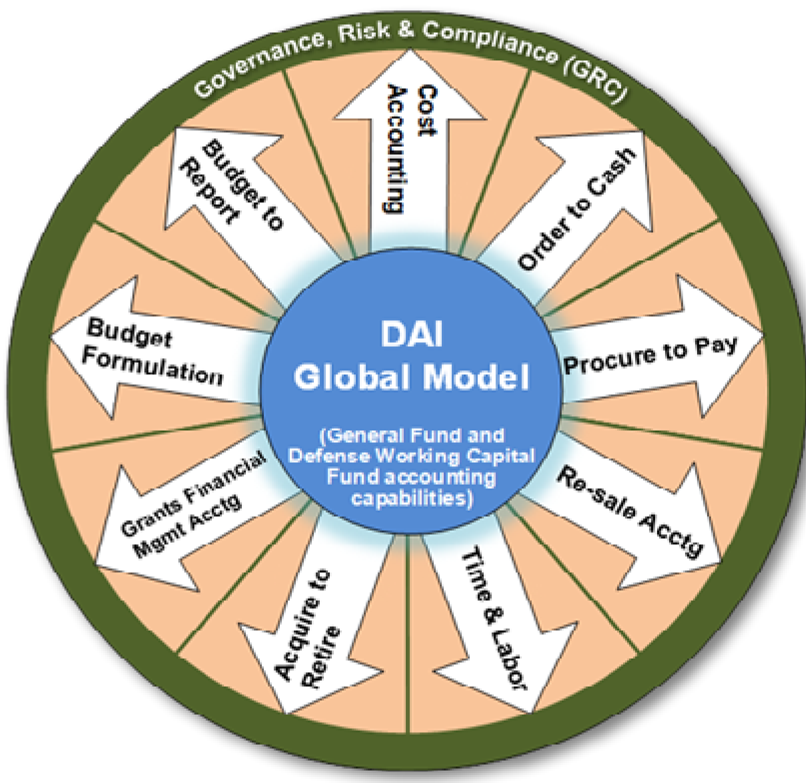



**Figure 16:** DAI's Nine Integrated Business Processes

For FY 2023, DAI targeted to provide assurance that:

- DAI implements and executes an auditable financial management system to support customer organizations' financial end-to-end processes. DAI received an unmodified opinion in a System and Organization Controls Type 2 report for the period October 1, 2022, through June 30, 2023 (latest available). (Targets O&M and RDT&E)

- DAI meets the 98.0% desired performance level objective for the system performance availability (i.e., % system is online and available to end users) and the 95.0% threshold for minimum acceptable performance. As displayed in Figure 17, DAI 2023 system availability exceeded the objective. (Targets O&M)

- DAI interfaces have data integrity checks in place to ensure no loss or corruption of data during transmission, as well as no loss of interoperability across business systems (i.e., timeliness and accuracy of data transfers) with a targeted objective of 98.0% and a 95.0% threshold. As displayed in Figure 17, DAI timeliness and accuracy for 2023 exceeded the objective. (Targets O&M and RDT&E)

- DAI successfully deployed Global Model capabilities to the DFAS and NSW in accordance with its implementation plan. (Targets O&M and RDT&E)

- DAI is implementing Global Model capabilities for CYBER Command (CYBERCOM) in accordance with its implementation plan. (Targets O&M and RDT&E)

In FY 2023, DAI received an unmodified opinion on all DAI control objectives design and operating effectiveness of the control objectives stated above. No adverse performance trends were identified during FY 2023. The reported performance information maps to the DAI Performance Baseline requirements. This information is regularly reviewed with using organizations and DAI leadership with a series of system technical reviews ending and Authorization to Proceed (ATP) decisions. The most recent DAI SOC-1 Type 2 report provides an unmodified opinion on all DAI control objectives design and operating effectiveness. During October 2024 DAI will migrate application hosting from DISA to commercial Cloud hosting. The shift to Cloud hosting is planned to improve scalability of the application to allow for growth in using organizations, maximize supportability and reduce cost.

| DAI Operating Metrics | | | | | | |
|---|---|---|---|---|---|---|
| | FY 2023 Threshold | FY 2023 Objective | FY 2023 Actual | FY 2022 Threshold | FY 2022 Objective | FY 2022 Actual |
| System Availability | 95.00% | 98.00% | 98.85% | 95.00% | 98.00% | 99.28% |
| Timeliness and Accuracy of Data Transfers | 95.00% | 98.00% | 99.77% | 95.00% | 98.00% | 99.70% |

**Figure 17:** DAI Operating Metrics

## DLA GF Performance Measure 3:
## O&M Defense Microelectronics Activity Program

This performance measure relates to the objective described above

***Objective 3.3:*** *Provide next generation customer service, including a customer feedback mechanism*

The Defense Microelectronics Activity (DMEA) uniquely accomplishes this mission for the Department by providing a guaranteed and trusted source of supply of microelectronics parts that are essential to combat operations. In addition, DMEA provides the rare technology and acquisition capabilities to develop, manage and implement innovative microelectronic solutions to enhance mission capability for customers across the department. DMEA provides decisive, quick turn solutions for defense, intelligence, special operations, cyber and combat missions, as well as microelectronic components that are unobtainable in the commercial market. DMEA accomplishes these missions by performing organic engineering services and production of microelectronic parts, acquisition of microelectronic foundry production, through the DMEA Trusted Access Program Office, accelerated acquisition of microelectronic development solutions in the defense industry utilizing the Advanced Technology Support Program, and leveraging the DMEA microelectronic manufacturing capabilities.

DMEA assists hundreds of Department programs every year. DMEA has provided its specialized engineering assistance and capabilities to older systems, current systems, and even to programs not yet in the production phase. This includes modernization efforts for the Space Awareness and Global Exploitation system, delivery of counter rocket, artillery and mortar and Counter Unmanned Aerial Systems missions to AFRICOM/CENTCOM/EUCOM/INDOPACOM, support to improve the effectiveness of counter Unmanned Aircraft Systems, prototype development of a B-2 Flight Control Computer, and Pacific Missile Range Facility Test Range improvements in support of Missile Defense Agency test missions among many other programs. DMEA assists the Combatant Commands including Special Operations, Cyber, Intelligence, and the Radiation-Hard communities.

## DLA GF Performance Measure 4:
## RDT&E Manufacturing Technology Program

This performance measure relates to the objectives described above

***Objective 1.1:*** *Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments;*
***Objective 1.2:*** *Partner with customers at the wholesale and retail levels to address Service- specific challenges and develop solutions;*
***Objective 1.3:*** *Proactively support the DoD Nuclear Enterprise and Space Enterprise;*
***Objective 2.1:*** *Implement a deliberate, enterprise- wide approach to Whole of Government support;*
***Objective 3.3:*** *Provide next generation customer service, including a customer feedback mechanism;*
***Objective 4.1:*** *Expand industry engagement to foster innovation and maximize value for our customers;*
***Objective 4.2:*** *Improve the end-to-end post-award segment to enable collaborative customer support, increase responsiveness, and manage costs;*
***Objective 4.3:*** *Develop a market intelligence capability to manage supply chain risk and drive best value;* ***Objective C.1:*** *Transformational information technologies capabilities;*
*and* ***Objective C.2:*** *Advanced Analytics and Automation*

The DLA GF ManTech program enables DLA to explore and develop innovative solutions to improve and modernize manufacturing processes directly aligned to the National Defense Strategy (NDS). The program aims to rebuild military readiness for a more lethal force and achieve reform through greater performance and affordability, predictive analytics, and continuous communication.

For FY 2023, DLA ManTech focused on the Battery Network (BATTNET), Subsistence Network (SUBNET), Advanced Microcircuit Emulation (AME), and Military Unique Sustainment Technology (MUST). The below highlights major completed projects within the programs:

## BATTNET Program

**Manufacturing Line Improvements for BA-5590 Batteries:**

- Enabled production enhancements and increase the surge capacity at a key supplier's lithium anode production line.
- Improved the product quality and performance of the high demand BA-5590 battery used on soldier systems and Wartime stock.

## SUBNET Program

**Utilization of Novel Processing Technology known as RF to Produce Commercially Sterile Low Acid Rations for Field Trials:**

- Demonstrated the quality improvements of Radio Frequency (RF) energy processed products over the conventional retort process and microwave energy.
- Submitted the findings to the FDA and produce samples for DLA in which quality will be compared in a field test to traditional retort processing.

## AME Program

**Dual-Port Memory Microcircuit Emulation Phase II:**

- Enhanced DLA Land and Maritime's Generalized Emulation of Microcircuits (GEM) program's existing memory microcircuit capability by adding the ability to produce microcircuits which can "read" and "write" data simultaneously.
- Provided microcircuits to our Services' weapons.
- Awarded a five-year task order (D-type) contract which allows rapid project initiation, as well as surge capabilities to support contingency operations.

## MUST Program

**Supply Request Package Tool (SRP) and Source Sampling Test Reporting Tool (SST):**

- Transitioned the SRP tool to production for new item introduction to DLA sustainment.
- SRP tool allows single point entry for all Services provided data to support future Service modernization initiative.
- SST tool changes item tests data results from manual submission to automate capability for use by DLA Troop Support Clothing and Textile vendors.


**Innovative Refueling Capability**

Senior Airman Anthony Bell, 31st Logistics Readiness squadron fuels service center controller demonstrates capabilities of the new Fluid Powered Additive Injector Carts concept to Mission Support Group leadership at Aviano Air Base, Italy, March 17, 2023. The new capability enables the 31st Fighter Wing to land at partner nation locations or commercial locations in Europe, that only have JET A1 fuel. The FPAIC will enable the team to blend Jet A1, or commercial grade fuel, with Fuel System Icing Inhibitor and enable non-stop flying operations for 31st Fighter Wing aircraft. (U.S. Air Force) **Photo by** Staff Sgt. Jessica Blair

## DLA GF Performance Measure 5:
## MILCON Military Construction

This performance measure relates to the objective described above

***Objective 1.1:*** *Improve end-to-end readiness and cost-effectiveness in support of Combatant Commander Campaign Plans and Integrated Contingency Plans in competitive and contested logistics environments*

The MILCON program provides funds for major construction to replace or renovate DoD fuel depots and Industrial Capabilities Program (ICP) facilities around the world. DLA GF sub-allots MILCON funds to various entities such as USACE and NAVFAC, which are DLA GF's primary design and construction agents for the MILCON program. Projects include fuel hydrant systems, numerous operations and HQ facilities, bulk fuel storage facilities, aircraft truck refill stations and government vehicle retail gas stations. For FY 2022 and FY 2023, NAVFAC was unable to provide reliable MILCON data due to a system migration, which is why the disclosures below pertain only to USACE for these years.

For FY 2023, the Facilities Modernization Division within Installation Management brought four USACE MILCON projects to completion as of September 30, 2023. The total value of this project was $43.4 million. The following figures summarize completed DLA MILCON projects.

**DLA MILCON Project Completion**
**-**
**Number of Projects Completed**

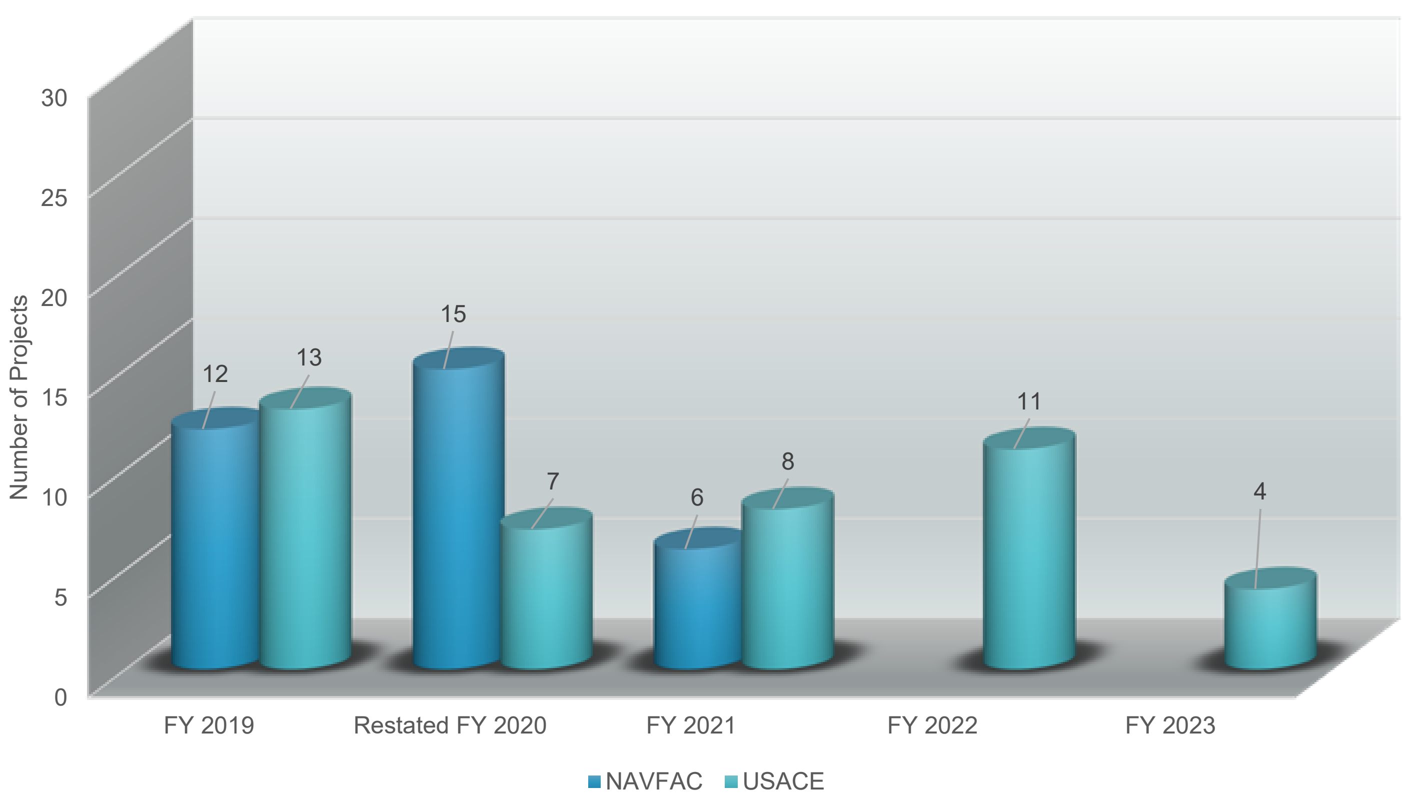



**Figure 18:** Completed DLA MILCON Projects by Year

# DLA MILCON Project Completion Value of Projects Completed

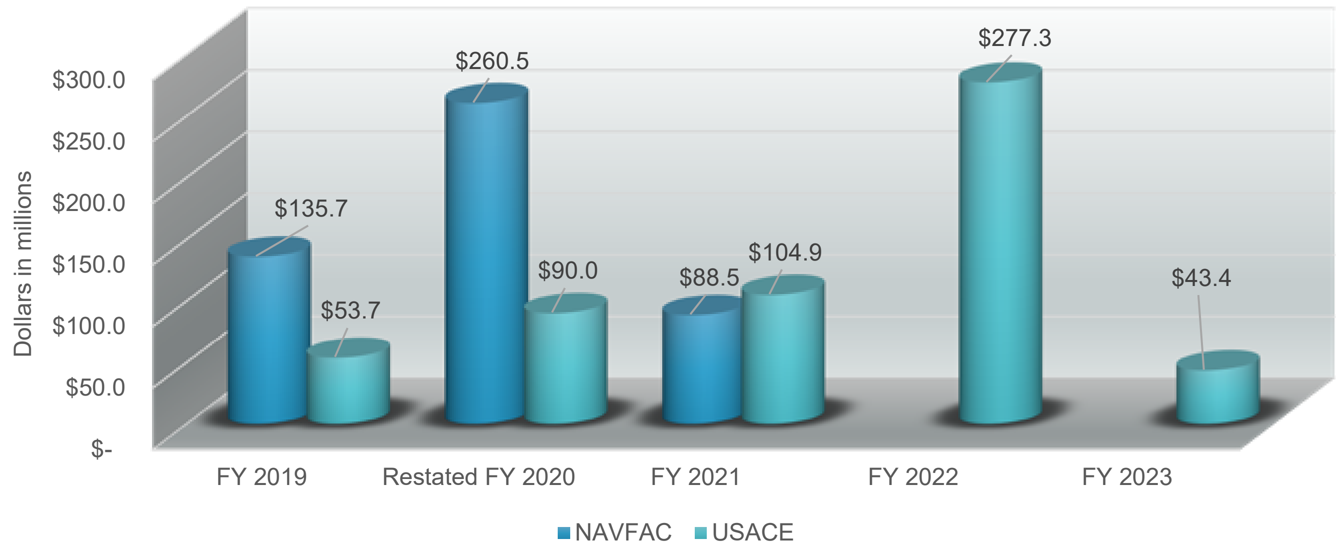



**Figure 19:** DLA MILCON Value of Completed Projects by Year

| MILCON Projects Completed in FY 2023 (Amounts in $) | | | | | |
|---|---|---|---|---|---|
| FY (Authorized) | Project Description | Installation / Location Name | Country | Quarter | Construction Cost |
| 2020 | Bulk Diesel System Replacement | McAlester, OK | USA | Q1 | $ 17,198,853 |
| 2019 | Refueling Facilities | Joint Base Lewis-McChord (Gray AFF), WA | USA | Q1 | 3,649,605 |
| 2019 | Replace Pol Pumphouse | Hill AFB, UT | USA | Q2 | 5,355,660 |
| 2016 | Main Access Control Point Upgrades | DLA Distribution, San Joaquin, CA | USA | Q3 | 17,155,654 |
| **FY 2023 Total** | | | | | **$ 43,359,772** |

**Figure 20:** Completed DLA MILCON Projects by Location

**Steel Knight Silhouette**
Marines observe impact zones during a fire support coordination exercise as part of Steel Knight, a combined arms live-fire exercise, at Marine Corps Air Ground Combat Center Twentynine Palms, Calif., Nov. 30, 2022. **Photo by:** Marine Corps Lance Cpl. Earik Barton

The DLA GF considers a MILCON project completed when the Construction in Process (CIP) ledger account has been reduced for the first time, reflecting the transfer of the asset to the receiving entity. Additional costs will continue to accrue in the CIP account after beneficial occupancy has occurred, while the construction contract work is being finalized. Once the contractor-submitted final invoice is paid and release of all claims has been confirmed, the project is readied for closure by the design and construction agent. A final Report of Transfer and Acceptance of Real Property (DoD Form DD1354) is produced at project closure, documenting all project costs.


### Completed DLA MILCON Projects

**First Row:** Expand Fire Department Facility, New Cumberland, PA

**Second Row:** Replace Fuel Storage & Distribution Facility, Fresno, CA

**Third Row:** Fuel Facilities Replacement, Columbus AFB, MS

**Fourth Row:** Ground Vehicle Fueling Facility Replacement, Joint Base Langley Eustis, VA

# National Defense Stockpile Transaction Fund

## DLA NDSTF Performance Measure 1:
DLA SM Sales versus Contract Awards

This performance measure relates to the objective described above

***Objective B2:*** *Cost visibility and cash management*

The DLA Strategic Materials (SM) targets current year sales to equal respective contract awards, as all the contracts signed each year are typically completed that year. SM cash receipts keep the program self-funded, facilitating program operations in current and future years.

The Stockpile Sales Program conducted 61 competitive offerings as of September 30, 2023. The 34 awarded sales contracts totaled $41.2 million, which is 82.8% of the $49.7 million FY 2023 award goal. Year to date, market conditions have led to fewer successful offerings versus FY 2022. Increased domestic supply of materials has pushed down quoted prices below calculated floor tolerances.

Any variances between contract awards and sales are typically due to timing of shipments; if a contract is signed late in the financial period the actual shipment (and the sales recognition) may be delayed until the following period.

## DLA SM Actual versus Contract Awards

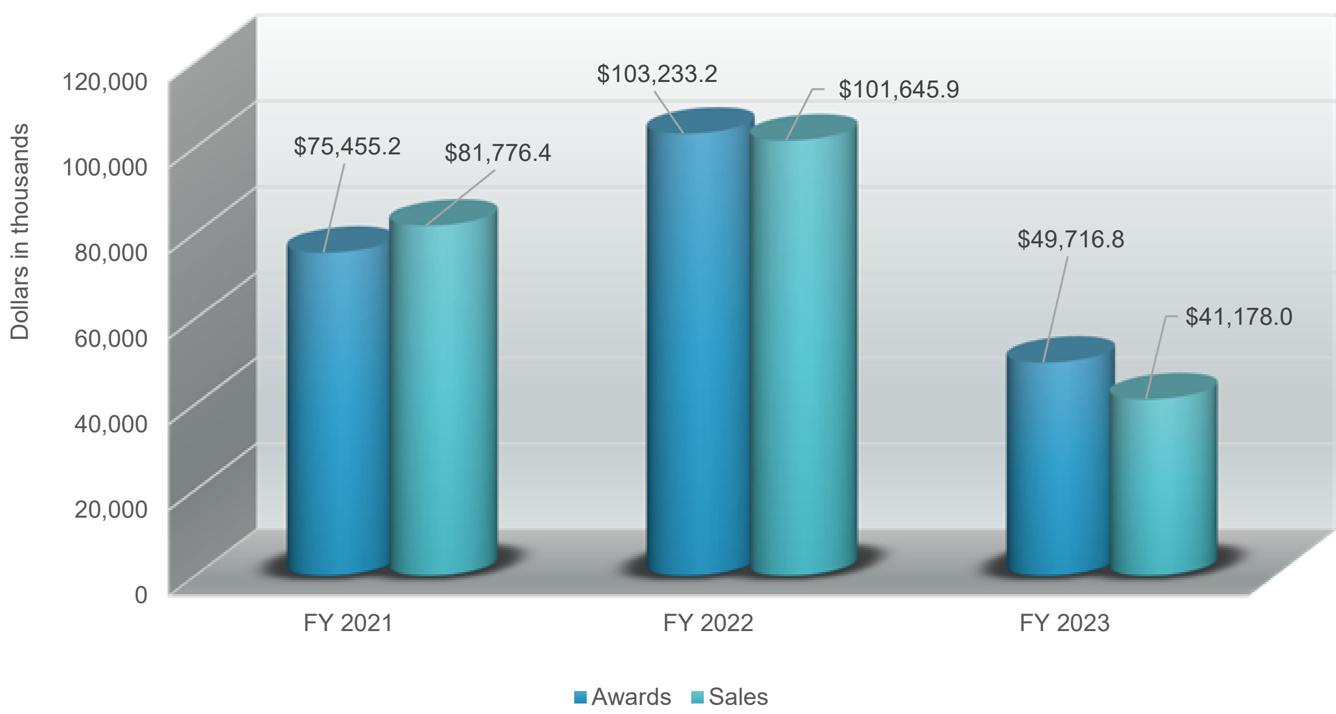



**Figure 21:** DLA SM Sales and Contract Awards

## DLA NDSTF Performance Measure 2:
## DLA SM Actual Collections versus Anticipated Collections

This performance measure relates to the objective described above

***Objective B2:*** *Cost visibility and management*

The DLA NDSTF is apportioned Spending Authority from Offsetting Collections to fund operational expenditures and strategic and critical materials purchases. Therefore, auditability hinges on metrics, controls and tracking over the movement of inventory, as it relates to disposals via public sales, and the corresponding accounting for the receipts of those sales to the NDSTF.

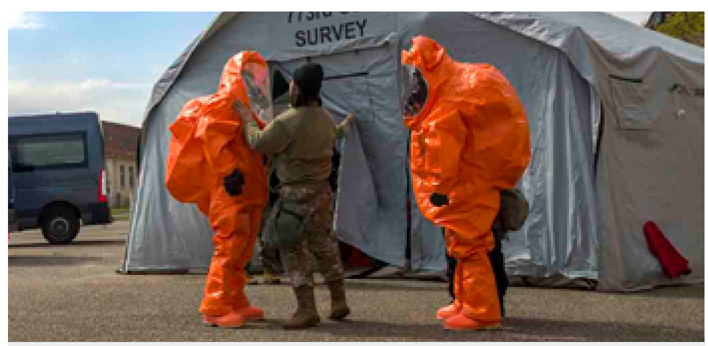
Through comprehensive analyses and study, all National Defense Stock (NDS) stocks undergo evaluation of need against a stringent set of criteria. The determinations from these analyses may result in authorization by Congress to acquire new materials and deem some current stocks excess. The National Defense Stock Piling Act provides authority for a public competitive sales program, which protects against an avoidable loss to the Government, and avoids undue disruption to the usual markets. The sale of excess stocks requires current existing legislative disposal authority along with an Annual Materials Plan (AMP). Congress typically provides disposal authority via the NDAA. Disposal authority, generally, provides quantity by material but does not always provide for a specific expiration. Additionally, the AMP provides for the ceiling limit quantity of any material sold in a given fiscal year.

The DLA SM operates the Stockpile Sales Program. DLA SM has built an established customer base. All approved and potential customers have undergone review for financial responsibility and have cleared a set of criteria for participation in the Stockpile Sales Program. DLA SM conducts on-going outreach and canvassing to the approved customer base and marketplace to determine business outlook and forecasting regarding demand for materials in order to issue public sales offerings. Pricing tolerances are established in advance based upon fair market value assessments to aid in protecting against avoidable loss. Awarded sales and terms are documented in a bilateral Sales Contract.

The DLA SM creates an Annual Sales Plan (ASP) to support the revenue projection as set forth in the Program Budget Review process. The ASP contains a mix of excess stocks, supported by the AMP believed to generate the anticipated collections authorized. Designated line items of inventory are made “available for sale” based on the ASP. These are the inventory items used to support sales offerings and generate revenue. Variances between the ASP and actual contract awards may occur due to market conditions. Collections are the result of execution under the sales contract terms. These collections serve to replenish the NDSTF and support revolving fund operations of the NDS.

FY 2023 collections totaled $40.9 million through September 30, or 82.0% of anticipated total year collections of $49.9 million.

In FY 2023, two types of contracts were awarded (fixed price and formula based), each with a period of performance between 30 and 90 days. Basic Ordering Agreement (BOA) sales contracts are fixed price and require payment and removal within 30 days. Negotiated contracts can be either fixed priced or formula based and up to 90 days in duration. As of September 30, 2023, there were 31 BOA’s and three Negotiated sales contracts awarded.




**Hot Zone**

Army Sgt. Tristan Abuyen and Spc. John DeJesus-Torres suit up to enter a simulated "hot zone" during an external evaluation exercise in Wiesbaden, Germany, April 18, 2023. **Photo by:** Army Staff Sgt. Jessica Forester

# DLA SM Actual Collections versus Anticipated Collections

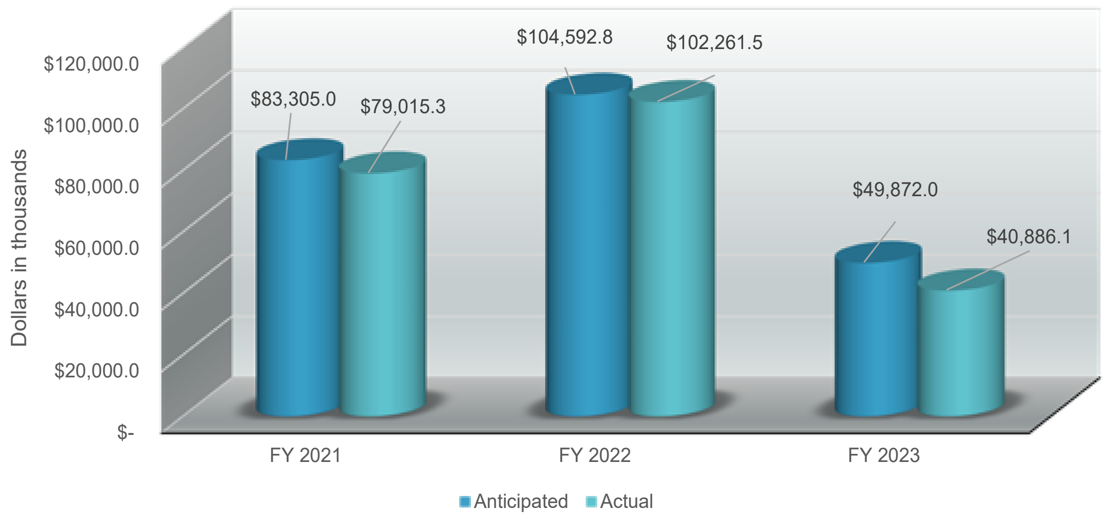



**Figure 22:** DLA SM Actual Collections versus Anticipated Collections

(From Standard Form 133, Report on Budget Execution and Budgetary Resources)

**Surgery Prep**

A soldier prepares for a mock surgery during medical training at Fort Sam Houston, Texas, Jan. 12, 2023. To ensure basic and critical medical and pharmaceutical needs are met, DLA support includes surgical items, preventive vaccines, field hospital equipment and even medical supplies for animals. **Photo by:** Tristin English, Air Force


## Replenishment Ready

Soldiers conduct sling load operations with a CH-47 Chinook on Oct. 10, 2022, at Petrochori Training Area, Greece. The United States' commitment to defending NATO territory is ironclad and the United States will continue to bolster our posture to better defend our NATO Allies. **Photo by:** Capt. Samuel Taylor, U.S. Army

# Analysis of Financial Statements and Stewardship Information

*This analysis presents a summary of DLA WCF, GF, and NDSTF financial position and results of operations and addresses the major changes and the related activity in the amounts of assets, liabilities, net position, cost, revenue, budgetary resources, and obligations.*

## WCF Overview Financial Position

The principal financial statements of DLA WCF include the Balance Sheets, Statements of Net Cost, Statements of Changes in Net Position, and the Combined Statements of Budgetary Resources. These principal financial statements and accompanying notes are included in the Financial Section of this AFR.

Preparing DLA WCF financial statements is a vital component of sound financial management and is intended to provide accurate, accountable, and reliable financial information that is useful for assessing performance, allocating resources, and for decision making on focus areas for future programmatic emphasis. DLA WCF's management is responsible for the integrity and objectivity of the financial information presented in the statements. DLA WCF is dedicated in its pursuit of financial management excellence.

A summary of DLA WCF's changes in key financial measures for FY 2023 and FY 2022 is presented in the following Analysis.

**Rocket lifts with DLA Energy Aerospace propellants**

Defense Logistics Agency Energy Aerospace provided the fuel to launch a United Launch Alliance Delta IV Heavy rocket carrying a payload for the National Reconnaissance Office from Vandenberg Space Force Base, California, Sept. 24. DLA Energy Aerospace Supplier Division provides the cradle-to-grave contracting support and award of government contracts for supplying liquid hydrogen and liquid oxygen to launch satellites and rockets. **Photo By:** United Launch Alliance

**Changes In Key Financial Measures**

As of and for the Years Ended September 30, 2023 and 2022 (dollars in millions)

**Condensed Principal Financial Statements**

| **Financial Condition** | **FY 2023** (Unaudited) | **FY 2022** (Unaudited) | **Increase/Decrease** $ | % |
|---|---|---|---|---|
| Fund Balance with Treasury | $ 5,102.4 | $ 4,702.9 | $ 399.5 | 8.5% |
| Accounts Receivable, Net and Other | 2,988.2 | 2,394.5 | 593.7 | 24.8% |
| Inventory and Related Property, Net | 23,985.0 | 23,931.1 | 53.9 | 0.2% |
| General PP&E, Net | 775.8 | 738.9 | 36.9 | 5.0% |
| Advances and Prepayments | 103.5 | 94.3 | 9.2 | 9.8% |
| **TOTAL ASSETS** | **$ 32,954.9** | **$ 31,861.7** | **$ 1,093.2** | **3.4%** |
| Accounts Payable | $ 3,515.2 | $ 2,916.5 | $ 598.7 | 20.5% |
| Environmental and Disposal Liabilities | 335.1 | 1,233.8 | (898.7) | -72.8% |
| Federal Benefits and Other Liabilities | 568.3 | 516.9 | 51.4 | 9.9% |
| Advances from Others and Deferred Revenue | 159.1 | 1,152.0 | (992.9) | -86.2% |
| **TOTAL LIABILITIES** | **$ 4,577.7** | **$ 5,819.2** | **$ (1,241.5)** | **-21.3%** |
| **TOTAL NET POSITION (ASSETS LESS LIABILITIES)** | **$ 28,377.2** | **$ 26,042.6** | **$ 2,334.6** | **9.0%** |
| Total Gross Cost | $ 45,842.8 | $ 43,746.5 | 2,096.3 | 4.8% |
| Less: Total Earned Revenue | (47,435.8) | (43,013.2) | (4,422.6) | 10.3% |
| **NET COST OF OPERATIONS** | **$ (1,593.0)** | **$ 733.3** | **$ (2,326.3)** | **-317.2%** |

**Figure 23:** Changes In Key Financial Measures

**Sunlit Patrol**

Soldiers conduct a dismounted patrol at the National Training Center at Fort Irwin, Calif., Jan. 27, 2023. **Photo by:** William Farrow, Army

# Financial Results Summary

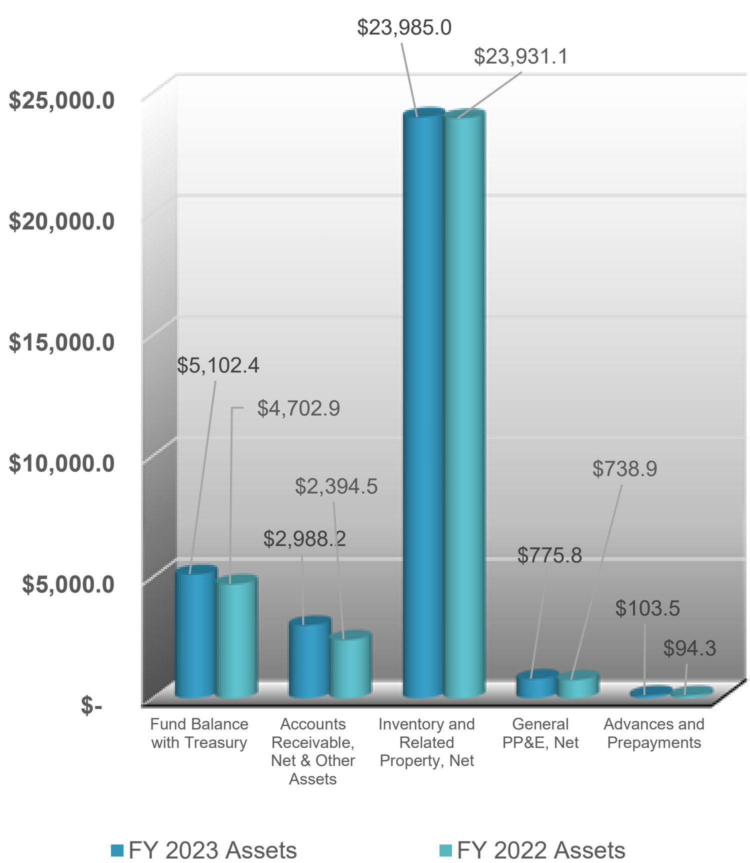
## Assets – What DLA WCF Owns and Manages

The DLA WCF owns and manages assets to accomplish its mission as the Nation's Combat Logistics Support Agency. These assets include Fund Balance with Treasury (FBwT), Accounts Receivable, Net and Other Assets, Inventory and Related Property, Net, Advances and Prepayments, and General PP&E. The DLA WCF Total Assets balance is $33.0 billion as of September 30, 2023.

Inventory and Related Property, Net, represents DLA WCF's largest asset with an amount of $24.0 billion or 72.8% of the WCF Total Assets as of September 30, 2023. Inventory and Related Property, Net consist of supply chain materials, equipment and repair parts, worldwide military supplies, and IH, primarily all held for sale. FBwT represented $5.1 billion or 15.5% of Total Assets as of September 30, 2023. FBwT increased by $399.5 million or 8.5% primarily due to an increase in collections as a result of the following: (1) DLA Energy actual product cost was less than the budgeted product cost, and (2) the receipt of appropriated funds for Red Hill efforts to be performed in FY 2024. Accounts Receivable increased by $593.7 million or 24.8% primarily due to increased billings related to a higher Cost Recovery Rate (CRR).

### Two Year Trend in Components of Total Assets (Unaudited)

As of September 30, 2023 and 2022 ($ in millions)




### Total Assets (Unaudited)

As of September 30, 2023 ($ in millions)

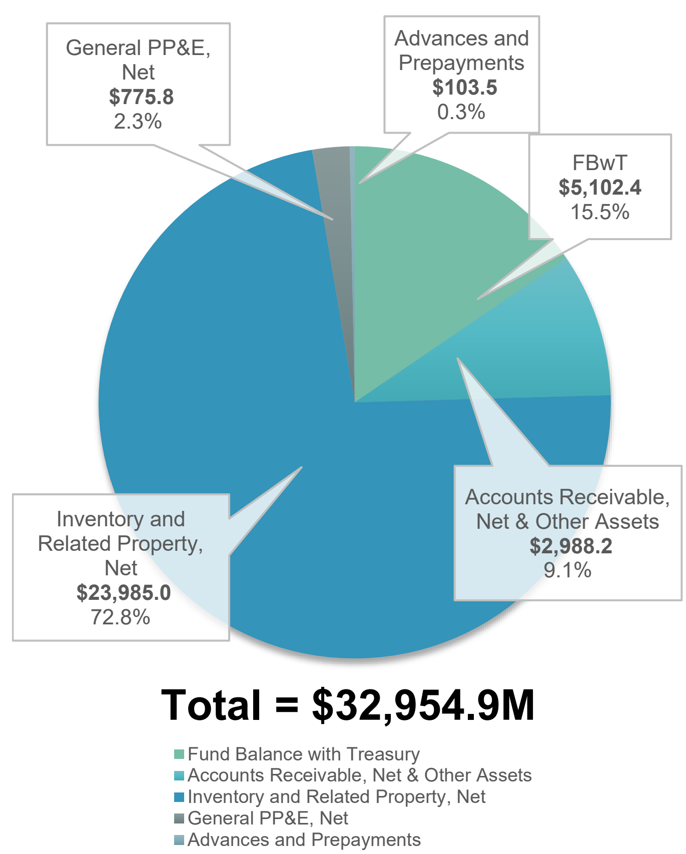



**Figure 24:** Total Assets by Component as of September 30, 2023 and 2022

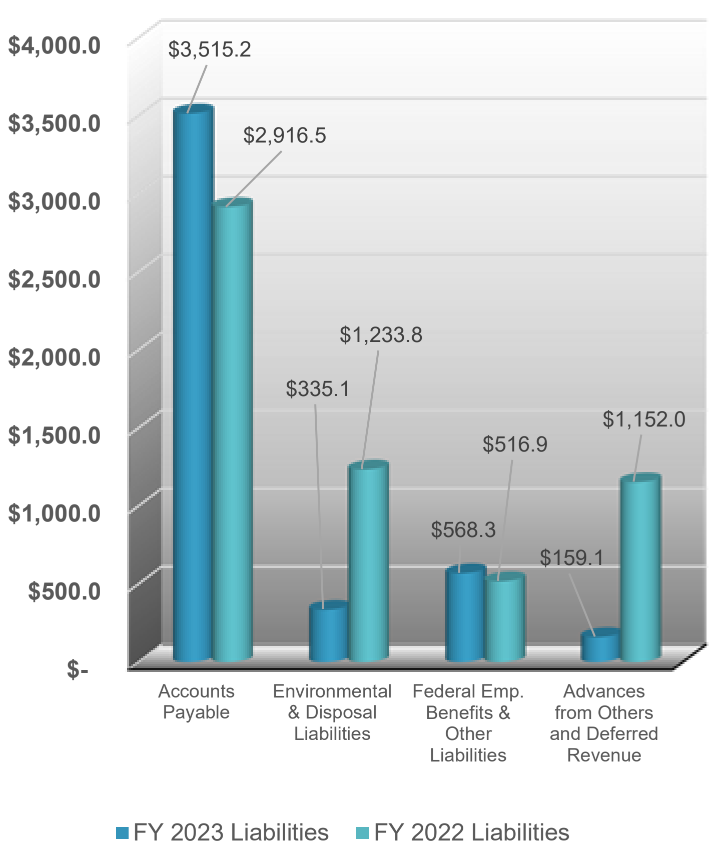
## **Liabilities** – What DLA WCF Owes

The DLA WCF liabilities are comprised of: (1) amounts owed to Federal and public entities for goods and services paid but not yet provided; (2) amounts owed to DLA WCF employees for wages and future benefits; (3) Environmental and Disposal Liabilities (E&DL); (4) Advances from Others and Deferred Revenue; and (5) Other Liabilities. The DLA WCF Total Liabilities balance is $4.6 billion as of September 30, 2023.

The DLA WCF primary liability is Accounts Payable with a balance of $3.5 billion or 76.8% of the WCF Total Liabilities. This balance increased by $598.7 million or 20.5%, primarily due to higher vendor payables at DLA Energy and Troop Support. Advances from Others and Deferred Revenue decreased by $992.9 million or 86.2%, primarily due to the decrease in COVID-19 related activities funded by the HHS as a result of the expiration of the public health emergency in FY 2023. E&DL decreased $898.7 million or 72.8% primarily due to the transfer of the liabilities to the Military Departments in accordance with DoD Financial Management Regulation (FMR) guidance based on Federal Accounting Standards Advisory Board (FASAB) Interpretation 9, *Cleanup Cost Liabilities Involving Multiple Component Reporting Entities: An Interpretation of SFFAS 5 & SFFAS 6*.

### Two Year Trend in Components of Total Liabilities (Unaudited)

As of September 30, 2023 and 2022 ($ in millions)




### Total Liabilities (Unaudited)

As of September 30, 2023 ($ in millions)

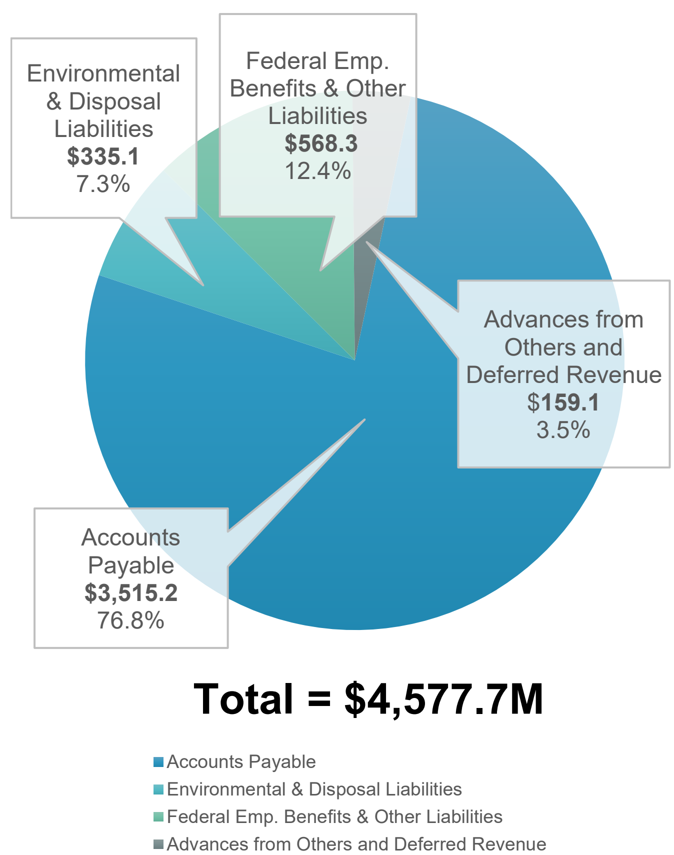



**Figure 25:** Total Liabilities by Component as of September 30, 2023 and 2022

## **Net Position** – What DLA WCF has Done Over Time

Net position represents the accumulation of revenue and expenses, and unexpended appropriations and other financing sources transferred in/out since inception, as represented in DLA WCF balances reflected in the Statements of Changes in Net Position. As of September 30, 2023, Total Net Position largely consisted of Cumulative Results of Operations of $27.7 billion, derived from producing goods and providing services for sale to Federal and public entities. This function is the primary source of sustaining DLA WCF in its key role of logistically supporting missions of America's Warfighters.

The net increase in Net Position of $2.3 billion or 9.0% from September 30, 2022 was largely attributable to increased Earned Revenue from sales of materials and services provided to customers.

## **Net Cost of Operations** – DLA WCF Net Operating Results

The DLA WCF operates under the mission of Sustain Warfighter readiness and lethality by delivering proactive global logistics in peace and war. DLA WCF has three activity groups: Energy, SCM, and Document Services. The three activity groups comprise a single, integrated business enterprise. For the year ended September 30, 2023, these three activity groups incurred Total Gross Cost of $45.8 billion and recognized Total Earned Revenue of $47.4 billion, respectively, resulting in Net Cost of Operations of ($1.6) billion. Net Cost of Operations decreased $2.3 billion due to an increase in Earned Revenue of $4.4 billion offset by an increase in Gross Cost of $2.1 billion. The increase in Earned Revenue was primarily due to higher product cost for DLA Energy Fuel Sales. The increase in Gross Cost was primarily due to an inflation-driven increase in the cost of inventory purchases, which caused a corresponding increase in the cost of goods sold.

**Two Year Trend in Gross Cost by Activity Group (Unaudited)**

For the Years Ended September 30, 2023 and 2022 ($ in millions)


**Total Gross Cost (Unaudited)**

For the Year Ended September 30, 2023 ($ in millions)

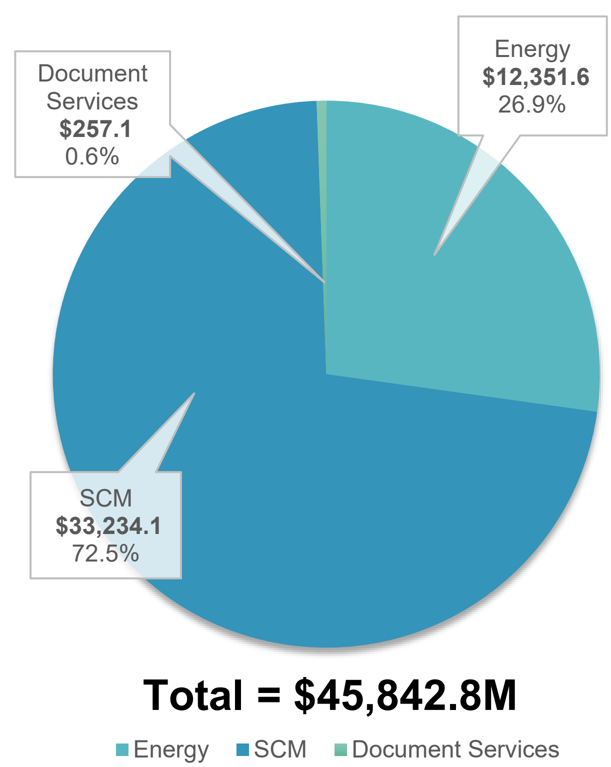
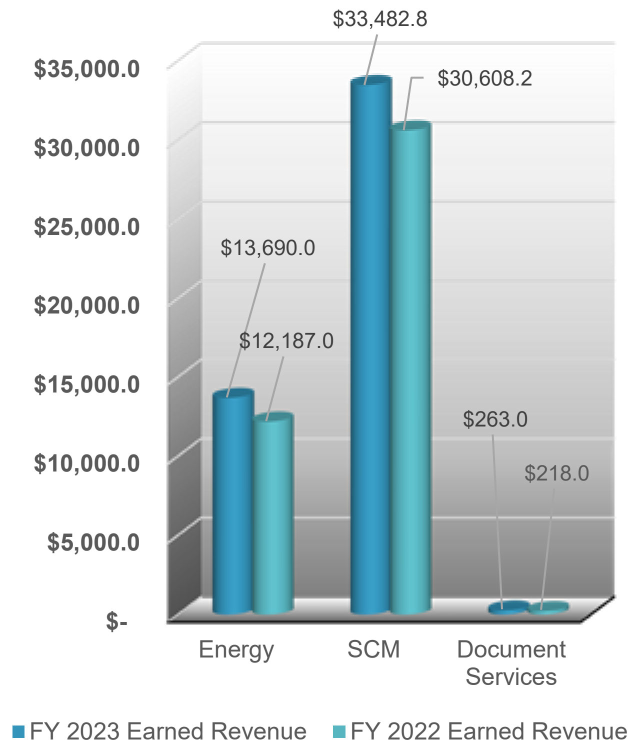



**Figure 26:** Gross Cost by Activity for the years ended September 30, 2023 and 2022

### Two Year Trend in Earned Revenue by Activity Group (Unaudited)

For the Years Ended September 30, 2023 and 2022 ($ in millions)




### Total Earned Revenue (Unaudited)

For the Year Ended September 30, 2023 ($ in millions)

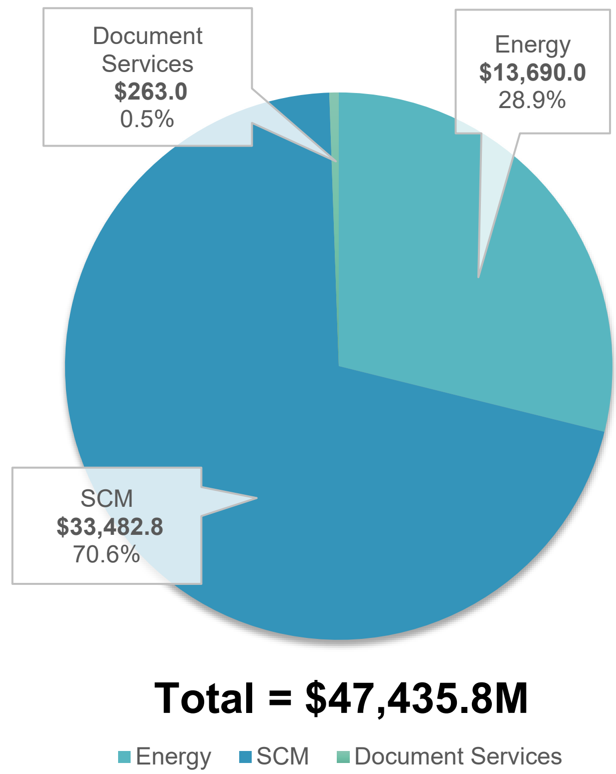



**Figure 27:** Earned Revenue by Activity for the years ended September 30, 2023 and 2022

**Over the Ocean**

An Air Force A-10C Thunderbolt II aircraft receives fuel from a KC-135 Stratotanker over the Atlantic Ocean, Feb. 28, 2023, while returning to Moody Air Force Base, Ga., from Operation Forward Tiger. The exercise conducted with Dominican and Jamaican forces is designed to increase combat readiness.

**Photo By:** DoD

## Budgetary Activity - DLA WCF Budgetary Resources and Obligations

The recognition of budgetary accounting transactions is essential for compliance with legal constraints and controls over the use of Federal funds. The budget represents the plan for efficiently and effectively achieving the strategic objectives to carry out the mission and to ensure that DLA WCF manages its operations within the appropriated amounts using budgetary controls. Two key components of budgetary activity include Budgetary Resources and Obligations. Budgetary resources are funds available to DLA WCF to incur obligations, to pay for goods and services, and to sell products to customers.

Obligations are balances for which there has been legally binding action during the year.

For the year ended September 30, 2023, Total Budgetary Resources were $58.7 billion and Total Obligations were $58.2 billion. Total Budgetary Resources increased $2.4 billion or 4.2% due to increased appropriations to support Red Hill recovery efforts in FY 2023.

Total New Obligations increased by $3.0 billion or 5.5% primarily due to increased obligation in DLA SCM-C&E, Aviation, Land and Maritime and Disposition, offset by adjustments related to COVID-19 relief efforts within SCM-Medical. In addition, Energy experienced an increase in obligations attributed to a significantly higher fuel purchase price.

### Two Year Trend in Status of Budgetary Resources and New Obligations (Unaudited)

For the Years Ended September 30, 2023 and 2022 ($ in millions)

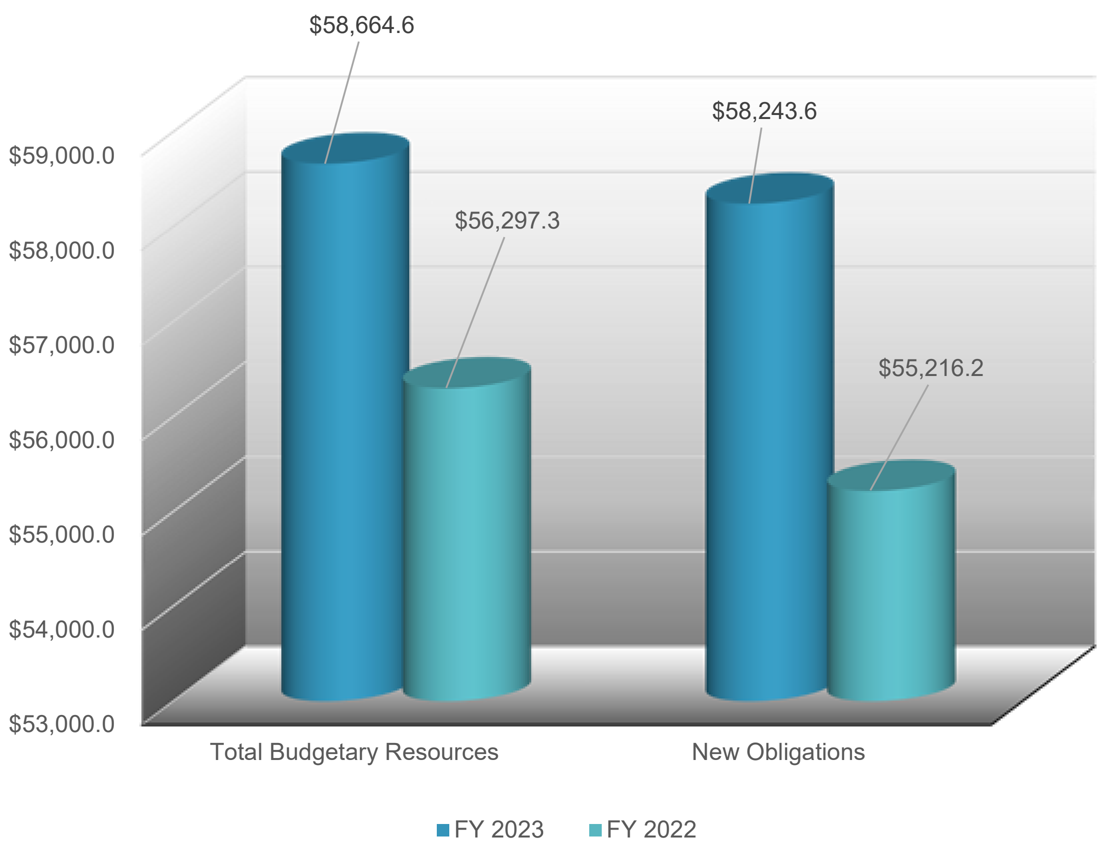



**Figure 28:** Total Budgetary Resources and New Obligations for the years ended September 30, 2023 and 2022

# GF Overview Financial Position

The principal financial statements of DLA GF include the Balance Sheets, Statements of Net Cost, Statements of Changes in Net Position, and the Combined Statements of Budgetary Resources. These principal financial statements and accompanying notes are included in the Financial Section of this AFR.

Preparing DLA GF financial statements is a vital component of sound financial management and is intended to provide accurate, accountable, and reliable financial information that is useful for assessing performance, allocating resources, and for targeting areas for future programmatic emphasis. DLA GF's management is responsible for the integrity and objectivity of the financial information presented in the statements. DLA GF is dedicated in its pursuit of financial management excellence.

A summary of DLA GF's changes in key financial measures for FY 2023 and FY 2022 is presented in the following Analysis of Key Financial Measures. The table represents assets on hand to pay liabilities, and the corresponding net position. The net cost of operations is the gross costs of DLA GF's five programs: O&M, PDW, RDT&E, Family Housing, and MILCON less earned revenue. Because of the materiality and nature of the program, DLA combines the Family Housing Program with MILCON for reporting purposes in the Statements of Net Cost. The Financial Results Summary section also includes an explanation of significant changes for each DLA GF financial statement.


**On the Course**

U.S. and Dutch marines prepare to drive during a tactical vehicle familiarization course at Marine Corps Air Ground Combat Center Twentynine Palms, Calif., Oct. 19, 2022. **Photo by:** Marine Corps Lance Cpl. Jonathan Willcox

## Changes In Key Financial Measures

As of and for the Years Ended September 30, 2023 and 2022 (dollars in millions)

**Condensed Principal Financial Statements**

| Financial Condition | FY 2023 (Unaudited) | FY 2022 Restated (Unaudited) | Increase/Decrease $ | Increase/Decrease % |
|---|---|---|---|---|
| Fund Balance with Treasury | $ 2,251.3 | $ 2,406.7 | $ (155.4) | -6.5% |
| General PP&E, Net | 526.9 | 392.3 | 134.6 | 34.3% |
| Inventory and Related Property, Net | - | 29.5 | (29.5) | -100.0% |
| Advances and Prepayments | 113.9 | 7.7 | 106.2 | 1,379.2% |
| Accounts Receivable and Other Assets | 14.9 | 13.9 | 1.0 | 7.2% |
| **TOTAL ASSETS** | **$ 2,907.0** | **$ 2,850.1** | **$ 56.9** | **2.0%** |
| Accounts Payable | $ 73.1 | $ 78.1 | $ (5.0) | -6.4% |
| Environmental and Disposal Liabilities | 76.4 | 78.3 | (1.9) | -2.4% |
| Federal Benefits and Other Liabilities | 14.8 | 12.5 | 2.3 | 18.4% |
| **TOTAL LIABILITIES** | **$ 164.3** | **$ 168.9** | **$ (4.6)** | **-2.7%** |
| **TOTAL NET POSITION (ASSETS LESS LIABILITIES)** | **$ 2,742.7** | **$ 2,681.2** | **$ 61.5** | **2.3%** |
| Total Gross Cost | $ 843.2 | $ 787.6 | $ 55.6 | 7.1% |
| Less: Total Earned Revenue | (76.2) | (78.8) | 2.6 | -3.3% |
| **NET COST OF OPERATIONS** | **$ 767.0** | **$ 708.8** | **$ 58.2** | **8.2%** |

**Figure 29:** Changes In Key Financial Measures

### Comfort Arrival

Hospital ship USNS Comfort (T-AH 20), is deployed to U.S. 4th Fleet in support of Continuing Promise 2022, a humanitarian assistance and good-will mission conducting direct medical care, expeditionary veterinary care, and subject matter expert exchanges with five partner nations in the Caribbean, Central and South America. **Photo by:** Mass Communication Specialist 2nd Class Juel Foster

# Financial Results Summary

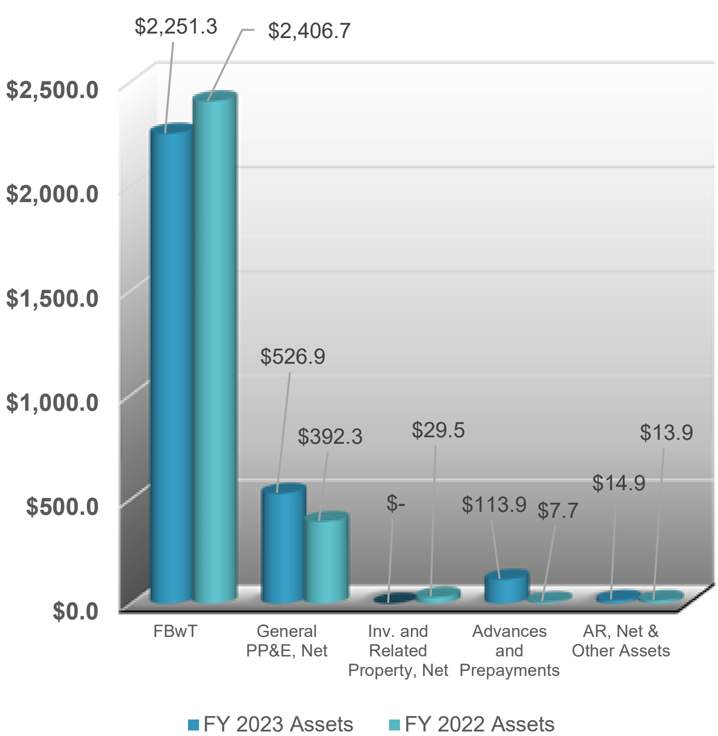
## Assets – What DLA GF Owns and Manages

The DLA GF owns and manages assets to accomplish its mission as the Nation's Combat Logistics Support Agency. These assets include: FBwT; General PP&E; Advances and Prepayments; and Accounts Receivable and Other Assets.

DLA GF's largest asset, FBwT, represented $2.3 billion or 77.4% of Total Assets as of September 30, 2023 and decreased by $155.4 million or 6.5%. The decrease was primarily due to increases in disbursements for the following programs: (1) PDW Application Specific Integrated Circuit (ASIC) Program inventory acquisitions transferred to the DLA WCF; and (2) O&M DAI, Continuity of Operations Program (COOP), Procurement Technical Assistance Program (PTAP), and Defense Property Accountability System (DPAS) program costs. DLA GF PP&E represented $526.9 million or 18.1% of Total Assets as of September 30, 2023 and is mostly comprised of CIP. The increase of $134.6 million or 34.3% is driven by increases in CIP projects constructed by NAVFAC and USACE. The increase in Advances and Prepayments of $106.2 million was due to contract financing for the PDW ASIC Program.

**Two Year Trend in Components of Total Assets (Unaudited)**

As of September 30, 2023 and 2022 ($ in millions)




**Total Assets (Unaudited)**

As of September 30, 2023 ($ in millions)

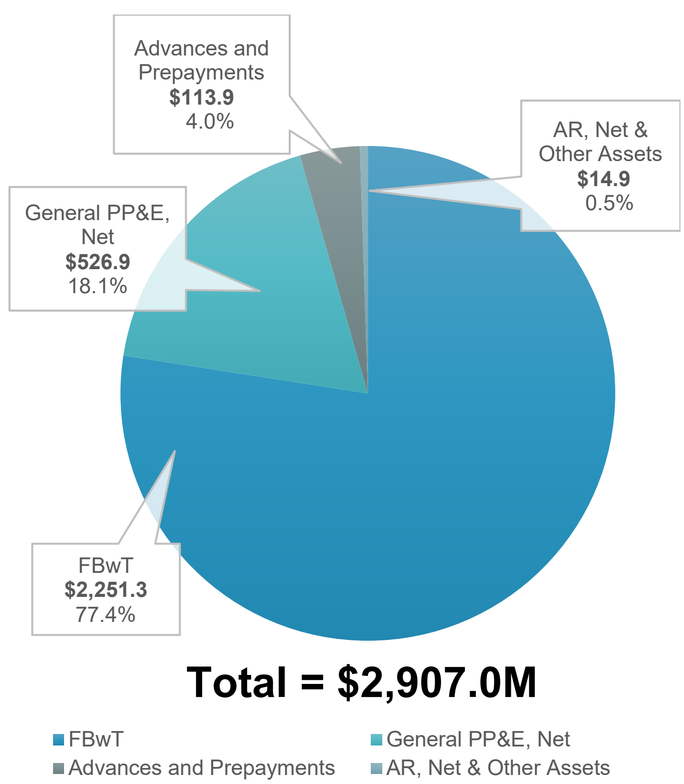



**Figure 30:** Total Assets by Component as of September 30, 2023 and 2022

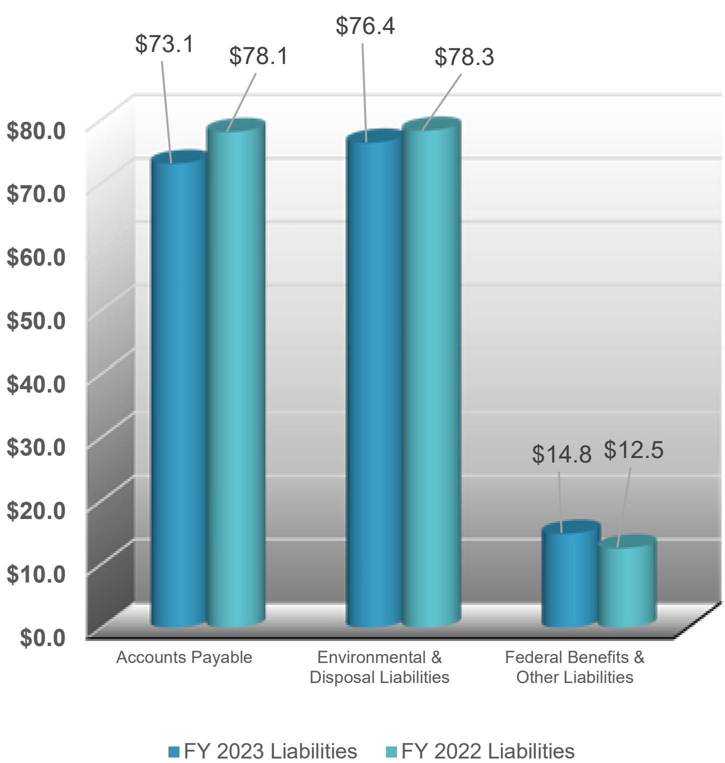
## **Liabilities** – What DLA GF Owes

DLA GF liabilities are comprised of amounts owed: (1) to Federal and public entities for goods and services provided but not yet paid; (2) to DLA GF employees for wages and future benefits; (3) for E&DL; and (4) for Other Liabilities. The largest DLA GF liability is E&DL with a balance of $76.4 million or 46.5% of Total Liabilities as of September 30, 2023.

Accounts Payable represented $73.1 million or 44.5% of Total Liabilities as of September 30, 2023. Federal Benefits and Other Liabilities represented $14.8 million or 9.0% of Total Liabilities as of September 30, 2023.

**Two Year Trend in Components of Total Liabilities (Unaudited)**

As of September 30, 2023 and 2022 ($ in millions)




**Total Liabilities (Unaudited)**

As of September 30, 2023 ($ in millions)

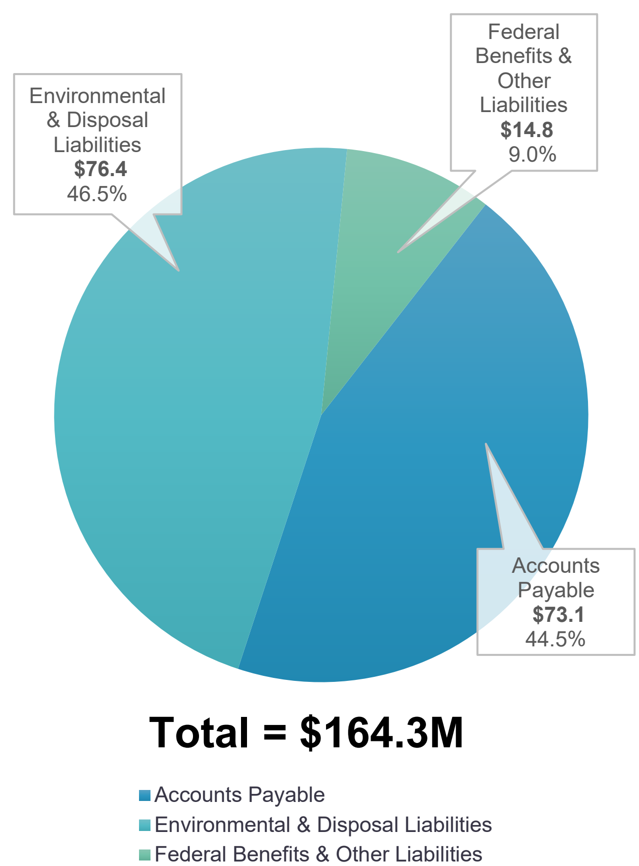



**Figure 31:** Total Liabilities by Component as of September 30, 2023 and 2022

## Net Position - What DLA GF Has Done Over Time

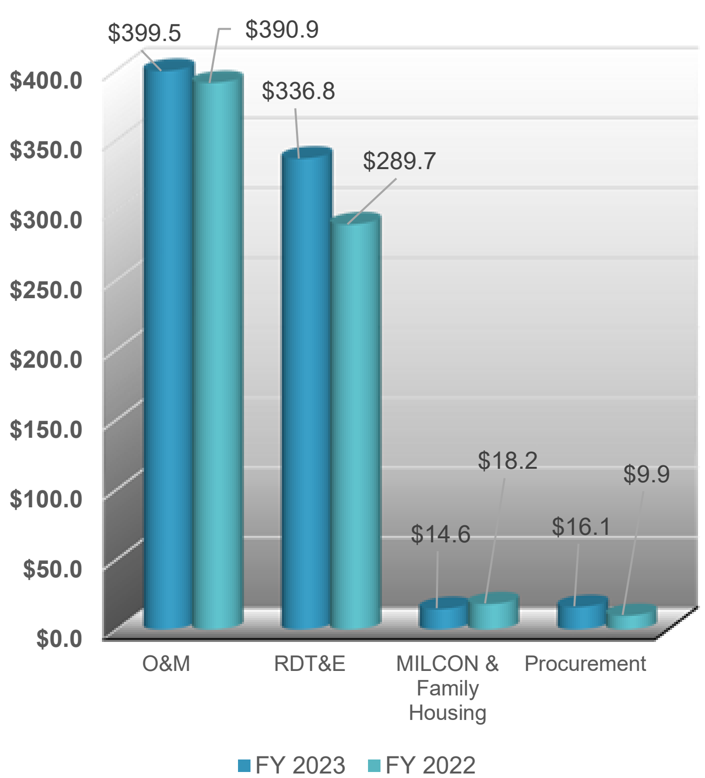
Net position represents the accumulation of Revenue and Expenses, and Unexpended Appropriations and Other Financing Sources transferred in/out since inception, as represented in DLA GF balances reflected in the Statements of Changes in Net Position. Total Net Position in the amount of $2.7 billion reported as of September 30, 2023 reflects an increase of $61.5 million or 2.3%. Net position is made of: (1) Unexpended Appropriations, and (2) Cumulative Results of Operations. Total Unexpended Appropriations decreased by $47.7 million or 2.0% due to decreases in appropriations for the PDW ASIC Program.

## Net Cost of Operations - DLA GF Net Operating Results

The DLA GF manages five programs: O&M, RDT&E, PDW, MILCON, and Family Housing. Net Cost is grouped by four major components, combining MILCON and Family Housing into one. For the year ended September 30, 2023, O&M represents the largest portion of Net Cost of Operations at $399.5 million. RDT&E represents the second largest portion of Net Cost of Operations at $336.8 million for the year ended September 30, 2023.

### Two Year Trend in Net Cost (Unaudited)

For the Years Ended September 30, 2023 and 2022 ($ in millions)




### Total Net Cost (Unaudited)

For the Year Ended September 30, 2023 ($ in millions)

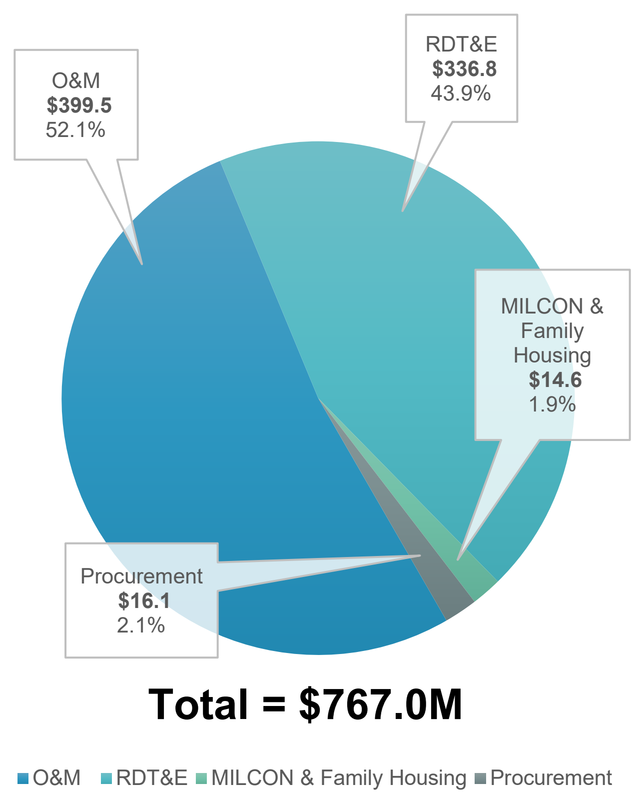



**Figure 32:** Comparative Net Cost by Program for the years ended September 30, 2023 and 2022

## **Budgetary Activity** - DLA GF Budgetary Resources and Obligations

The recognition of budgetary accounting transactions is essential for compliance with legal constraints and controls over the use of Federal funds. The budget represents the plan for efficiently and effectively achieving the strategic objectives to carry out the mission and to ensure that DLA GF manages its operations within the appropriated amounts using budgetary controls. Two key components of budgetary activity include Budgetary Resources and Obligations. Budgetary resources are funds available for DLA GF to incur obligations to pay for goods and services prior to the cancellation of funds.

Obligations are balances for which there has been legally binding action during the year.

For the year ended September 30, 2023, DLA GF's Total Budgetary Resources were $1.8 billion and New Obligations and Upward Adjustments totaled $1.2 billion.

The decrease of appropriations in FY 2023 for the PDW ASIC Program resulted in decreases to Total Budgetary Resources of $319.4 million or 15.2%, and New Obligations and Upward Adjustments of $290.2 million or 19.5%.

### Two Year Trend in Status of Budgetary Resources and Obligations(Unaudited)

For the Years Ended September 30, 2023 and 2022 ($ in millions)

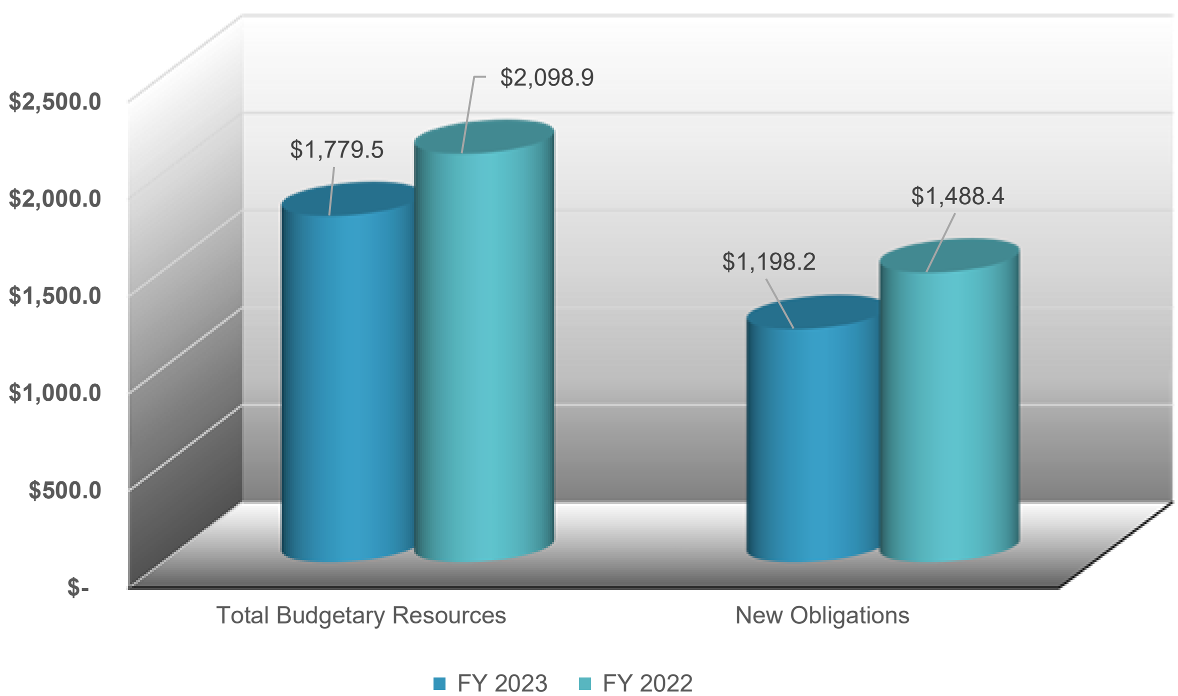



**Figure 33:** Status of Budgetary Resources for the years ended September 30, 2023 and 2022

# NDSTF Overview Financial Position

The principal financial statements of DLA NDSTF include the Balance Sheets, Statements of Net Cost, Statements of Changes in Net Position, and the Statements of Budgetary Resources. These principal financial statements and accompanying notes are included in the Financial Section of this AFR.

Preparing DLA NDSTF financial statements is a vital component of sound financial management and is intended to provide accurate, accountable, and reliable financial information that is useful for assessing performance, allocating resources, and for targeting areas for future programmatic emphasis. DLA NDSTF's management is responsible for the integrity and objectivity of the financial information presented in the statements. DLA NDSTF is dedicated in its pursuit of financial management excellence.

A summary of DLA NDSTF's changes in key financial measures for FY 2023 and FY 2022 is presented in the following Analysis of Key Financial Measures. The table represents the assets on hand to pay liabilities, and the corresponding net position. The net cost of operations is the gross costs of executing DLA NDSTF programs, less earned revenue. The Financial Results Summary section also includes an explanation of significant changes for each DLA NDSTF financial statement.


**Debris Removal**

Stetson Smith, a civil engineer from the Vicksburg District for the Army Corps of Engineers, left, and 1st Lt. Briana Karayinopulos, a project manager from the New England District for the USACE, discuss technical debris assistance in Lee County, Fort Meyers, Fla., Oct. 12, 2022. **Photo by:** Patrick Moes, Army

**Changes In Key Financial Measures**

As of and for the Years Ended September 30, 2023 and 2022 (dollars in millions)

**Condensed Principal Financial Statements**

| **Financial Condition** | **FY 2023** (Unaudited) | **FY 2022** (Unaudited) | **Increase/Decrease** $ | **Increase/Decrease** % |
|---|---|---|---|---|
| Fund Balance with Treasury | $ 579.8 | $ 500.6 | $ 79.2 | 15.8% |
| Inventory and Related Property, Net | 384.7 | 762.6 | (377.9) | -49.6% |
| General PP&E, Net | 0.4 | 0.6 | (0.2) | -33.3% |
| Advances and Prepayments | 25.5 | 1.5 | 24.0 | 1,600.0% |
| **TOTAL ASSETS** | **$ 990.4** | **$ 1,265.3** | **$ (274.9)** | **-21.7%** |
| Accounts Payable | $ 0.8 | $ 1.5 | $ (0.7) | -46.7% |
| Environmental and Disposal Liabilities | 11.7 | 12.2 | (0.5) | -4.1% |
| Federal Benefits and Other Liabilities | 3.0 | 2.7 | 0.3 | 11.1% |
| Advances from Others and Deferred Revenue | - | 0.6 | (0.6) | -100.0% |
| **TOTAL LIABILITIES** | **$ 15.5** | **$ 17.0** | **$ (1.5)** | **-8.8%** |
| **TOTAL NET POSITION (ASSETS LESS LIABILITIES)** | **$ 974.8** | **$ 1,248.3** | **$ (273.5)** | **-21.9%** |
| **Total Liabilities and Net Position** | **$ 990.4** | **$ 1,265.3** | **$ (274.9)** | **-21.7%** |
| Total Gross Cost | $ 577.9 | $ 90.0 | $ 487.9 | 542.1% |
| Less: Total Earned Revenue | (190.3) | (101.7) | (88.6) | 87.1% |
| **NET COST OF OPERATIONS** | **$ 387.6** | **$ (11.7)** | **$ 399.3** | **3,412.8%** |

**Figure 34:** Changes In Key Financial Measures


### Fuel Point Project

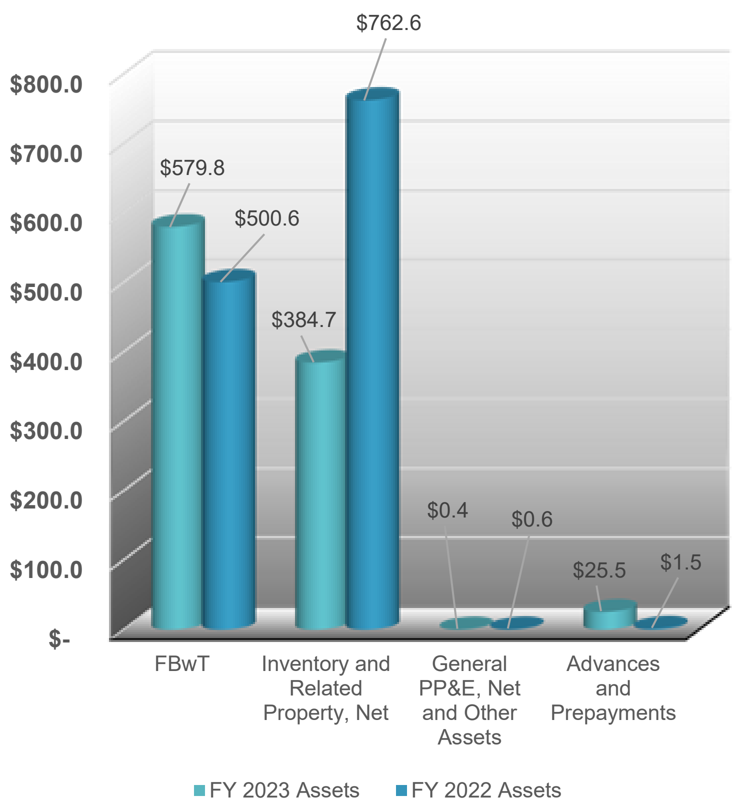
A Defense Logistics Agency Energy contractor completes electrical hookups June 2 for temporary fuel storage tanks delivered to Defense Supply Center Columbus the day before. The temporary tanks will ensure seamless fuel point operations for military and installation customers while a project to replace the existing underground storage tanks is underway. The underground tanks are now beyond their useful life. **Photo by:** Shannon Mormon/DSCC

# Financial Results Summary

## **Assets** – What DLA NDSTF Owns and Manages

The DLA NDSTF owns and manages assets to accomplish its mission as the Nation's Combat Logistics Support Agency. These assets include FBwT, Inventory and Related Property, General PP&E and Other Assets, and Advances and Prepayments. DLA NDSTF's largest asset is FBwT, which represents $579.8 million or 58.6% of Total Assets as of September 30, 2023. The FBwT increase of $79.2 million or 15.8% was largely due to appropriations received of $93.5 million under the Public Law 117-180. Inventory and Related Property decreased by $377.9 million or 49.6% due to valuation adjustments of $328.3 million. Advances and Prepayments increased by $24.0 million due to a research project for which stockpile materials were paid for but not yet received.

**Total Assets (Unaudited)**
As of September 30, 2023 and 2022 ($ in millions)




**Total Assets (Unaudited)**
As of September 30, 2023 ($ in millions)

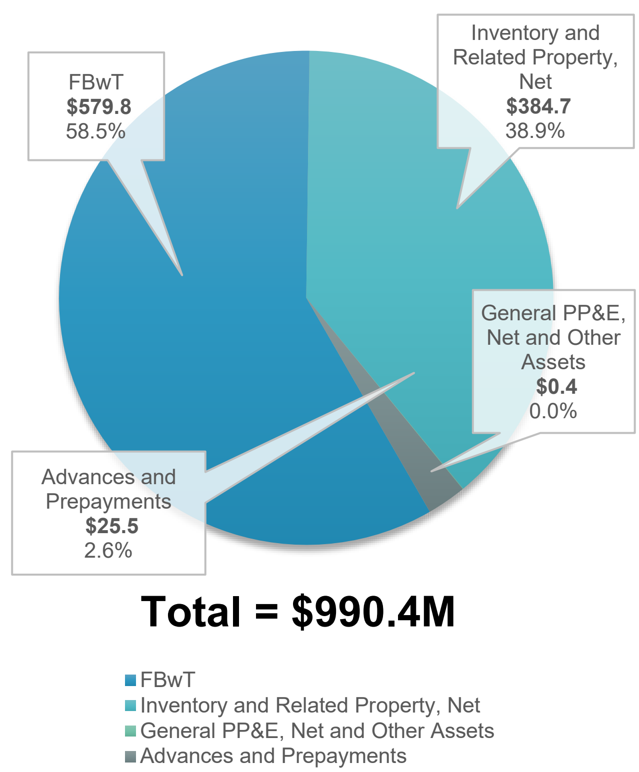


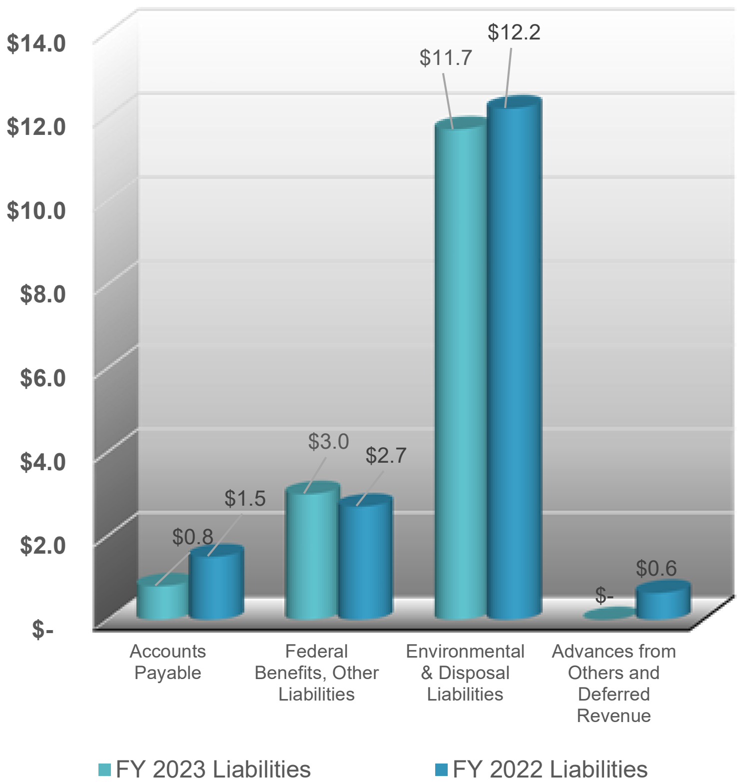

**Figure 35:** Total Assets by Component as of September 30, 2023 and 2022.

## Liabilities - What DLA NDSTF Owes

DLA NDSTF liabilities are comprised of amounts owed: (1) to Federal and public entities for goods and services provided but not yet paid; (2) to DLA NDSTF employees for wages and future benefits; and (3) for E&DL. The largest liability is E&DL, which represents $11.7 million or 75.5% of the Total Liabilities of $15.5 million as of September 30, 2023. Federal Benefits and Other Liabilities of $3.0 million represent 19.34% of DLA NDSTF's Total Liabilities as of September 30, 2023. Accounts Payable represents $0.8 million or 5.1% of Total Liabilities as of September 30, 2023.

### Two Year Trend in Components of Total Liabilities (Unaudited)

As of September 30, 2023 and 2022 ($ in millions)




### Total Liabilities (Unaudited)

As of September 30, 2023 ($ in millions)

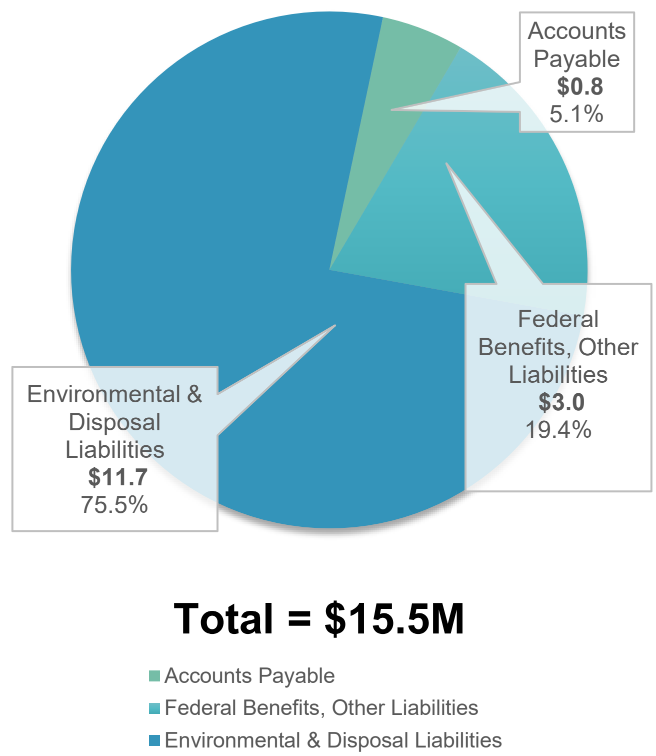



**Figure 36:** Total Liabilities by Component as of September 30, 2023 and 2022.

## **Net Position -** What DLA NDSTF has Done Over Time

Net position represents primarily the accumulation of revenue and expenses, as represented in DLA NDSTF balances reflected in the Statements of Changes in Net Position. DLA NDSTF Net Position primarily consisted of Cumulative Results of Operations of $738.3 million and $1,123.3 million as of September 30, 2023 and 2022, respectively. DLA NDSTF Net Position also includes Unexpended Appropriations of $236.6 million and $125.0 million as of September 30, 2023 and 2022 comprised of appropriations under Public Laws 117-180 and 117-103, respectively.

## **Net Cost of Operations -** DLA NDSTF Net Operating Results

The DLA NDSTF Statements of Net Cost reports one program: Operations, Readiness, and Support. Net Cost of Operations totaled $387.6 million and ($11.7) million for the years ended September 30, 2023 and 2022. Net Cost of Operations increased by $399.3 million primarily due to an increase in net losses as a result of stockpile material valuation adjustments.

## **Budgetary Activity -** DLA NDSTF Budgetary Resources and Obligations

The recognition of budgetary accounting transactions is essential for compliance with legal constraints and controls over the use of Federal funds. The budget represents the plan for efficiently and effectively achieving the strategic objectives to carry out the mission of DLA and to ensure that DLA NDSTF manages its operations within the appropriated amounts using effective budgetary controls. Two key components of budgetary activity include Budgetary Resources and Obligations. Budgetary resources are funds available to DLA NDSTF to incur obligations, to pay for goods and services, and to sell products to customers. Obligations are balances for which there has been legally binding action during the year.

For the year ended September 30, 2023, Total Budgetary Resources are $585.8 million, and Obligations are $131.5 million. Total Budgetary Resources increased by $102.8 million or 21.3%, which was primarily due to appropriations received of $93.5 million under the Public Law 117-180. New Obligations increased by $76.9 million or 140.8% due to the procurement of stockpile materials for a research project.

### Two Year Trend in Status of Budgetary Resources and Obligations(Unaudited)

For the Years Ended September 30, 2023 and 2022 ($ in millions)

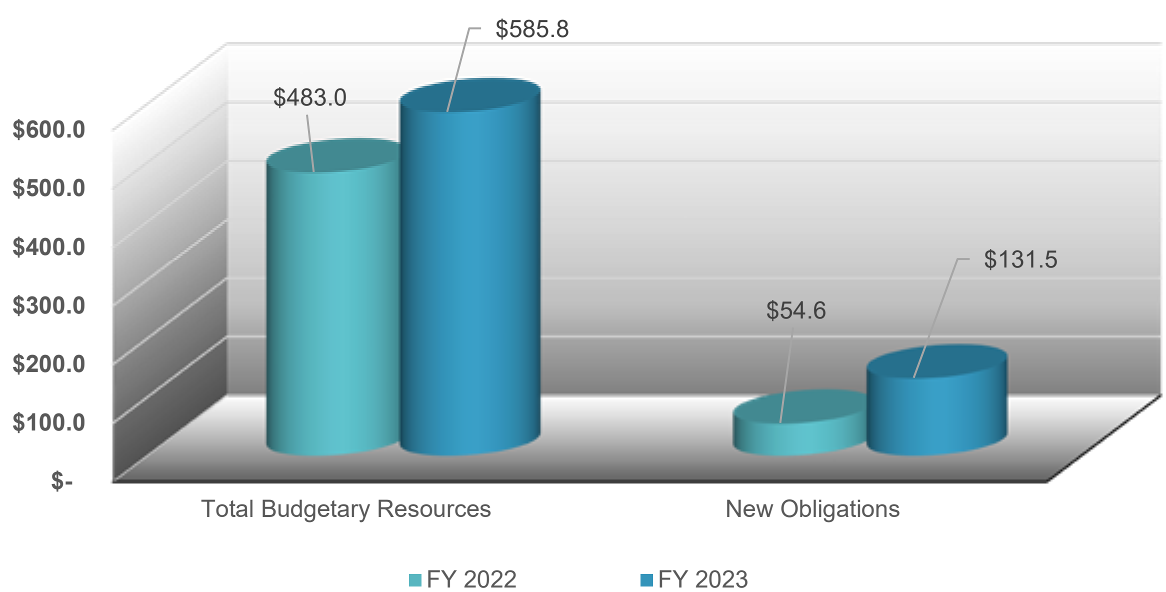



**Figure 37:** Total Budgetary Resources and New Obligations for the years ended September 30, 2023 and 2022.

# Limitations of the Financial Statements

The DLA WCF, GF, and NDSTF principal financial statements[2] and accompanying notes are prepared to report the financial position and results of operations of DLA WCF, GF, and NDSTF, as required by the CFO Act of 1990, expanded by the GMRA of 1994, and 31 U.S.C. § 3515(b).

The DLA WCF, GF, and NDSTF are unable to fully implement all elements of U.S. GAAP as promulgated by the Federal Accounting Standards Advisory Board (FASAB) and the form and content requirements for Federal government entities specified by OMB Circular A-136 and other authoritative guidance. This is due to financial and nonfinancial management system limitations, as well as limitations on the underlying processes that support the principal financial statements. DLA WCF, GF, and NDSTF derive reported values and information for major asset and liability categories largely from nonfinancial 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 U.S. GAAP. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by U.S. GAAP, and most of the financial management systems used by DLA WCF, GF, and NDSTF were designed to record information on a budgetary basis.

The DLA continues to address IT and financial audit NFRs to strengthen system controls and financial and regulatory compliance with corrective action plans that include developing requests for systems changes. DLA has begun migrating to the 4th version of System Applications and Products (SAP's) Data processing Enterprise Resource Planning (ERP) Business Suite 4 SAP HANA (SAP S/4HANA). Phase 1 of the two phased ERP Migration has been completed and Phase 2 is currently in process, with a planned completion date of FY 2027. SAP S/4 will provide enhanced reporting of financial information on the full accrual accounting basis and streamline data between IT systems, which DLA continues to consolidate and rationalize through the migration of major legacy systems.

The DLA WCF, GF, and NDSTF continue to develop, improve, and refine the underlying financial and nonfinancial end-to-end processes and systems that support the compilation of the financial statements and notes in accordance with U.S. GAAP as promulgated by FASAB and other Federal regulations. DLA WCF, GF, and NDSTF continue to implement interim mitigation processes to address known limitations; additionally, DLA WCF, GF, and NDSTF are remediating material weaknesses to the financial statement preparation process. DLA WCF, GF, and NDSTF have several corrective actions underway intended to improve the underlying systems, business processes and internal controls.

The financial statements should be read with the realization that they are for a component of the U.S. Government.

[2] Refer to the Financial Section Introduction for definition of principal financial statements.

# Analysis of Systems, Controls, and Legal Compliance

The DLA management is responsible for establishing, maintaining, and assessing internal controls to provide reasonable assurance that the objectives of OMB Circular A-123, Management's Responsibility for Enterprise Risk Management (ERM) and Internal Control, the FMFIA (31 U.S. Code (U.S.C.) 3512, Sections 2 and 4), and the FFMIA (Pub. L. 104-208), as prescribed by U.S. Government Accountability Office (GAO) Green Book, *Standards for Internal Control in the Federal Government*, are met.

The appendices referenced within the annual Statement of Assurance (SOA) below are OMB Circular A-123 appendices and are not included in the DLA AFR.

# Management Assurances

DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD
FORT BELVOIR, VIRGINIA 22060-6221

July 19, 2023

MEMORANDUM FOR VICE ADMIRAL MICHELLE C. SKUBIC, DIRECTOR, DLA

SUBJECT: Major Management and Performance Challenges Facing the Defense Logistics Agency

This year the Office of the Inspector General (OIG) has aggregated the major management and performance challenges facing DLA into three general topics: Business Process Documentation and Internal Controls, Data Management, and Property Accountability. We also identified two risks that were not related to one of the forementioned consolidated risk topics. The general risk topics are discussed below.

**Business Process Documentation and Internal Controls:** This area highlights the need for adequate business process documentation, internal controls, and complementary user entity controls for all DLAs business processes. DLA OIG is in the process of completing a series of projects reviewing the steps taken to ensure that DLA obtains an unmodified opinion on all its financial statements. Generally, we are finding that the basic, foundational business process and internal control documentation is inadequate or non-existent.

**a. Audit Documentation:** DLA OIG is in the process of completing a series of projects reviewing the steps taken to ensure DLA obtains an unqualified opinion to confirm our financial statements are fair and appropriately represented. Generally, we are finding that the basic, foundational business process and internal control documentation is missing. In 2022 we documented this challenge as DLA attempted to minimize the number of future notices of finding and recommendation (NFR) from our public accountant, as well as address existing NFRs. We have not seen sufficient progress on this risk. Without accurate and detailed business process flowcharts and descriptions (including formal policy and implementing procedures), external auditors cannot quickly and easily understand the process and DLA cannot prove that the correct internal controls have been developed. Business process documentation must address inputs received from other processes, identification of risks associated with a process, management’s evaluation and/or acceptance or addressing of the risk, the implementation of associated internal controls, and the output(s) to other business processes. Until this is achieved, DLA will continue receiving numerous NFRs and the external auditor will continue to deem corrective actions inadequate.

**b. Sales of DoD Property:** DLA still needs to establish sufficient policy and oversight of DLA sales of property in policy. This concern was formally recognized in a finding in FY18 during an Agency Management Review and has not been corrected to date. While multiple components of DLA are involved in the sales of DoD property, DLA Headquarters has limited expertise within the staff to develop adequate policy. Additionally, sales procedures and process are impacted by law and rules from several governmental agencies. Inadequate agency and MSC policy and the lack of execution oversight by DLA remains an area of risk that requires mitigation and remediation and clear documentation in the business process.

**Data Management:** The need for DLA to begin using the significant amount of data that exists within the data warehouse to make appropriate inventory purchase and stockage decisions go hand in hand with business process documentation and internal controls management. Specifically highlighting the risk of single point of failure and just-in-time inventory.

DEFENSE LOGISTICS AGENCY
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8725 JOHN J. KINGMAN ROAD
FORT BELVOIR, VIRGINIA 22060-6221

July 19, 2023

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### Transporting Equipment

Army Sgt. Jonathan Campbell, assigned to the 51st Composite Truck Company, 18th Combat Sustainment Support Battalion, 16th Sustainment Brigade, tightens a rig for heavy equipment transportation during Orion 23 in Camp De Mailly, France, April 23, 2023. **Photo By:** Courtesy of U.S. Army

# Summary of Internal Control

*The objectives of the system of internal control of DLA are to provide reasonable assurance of:*

- **Effectiveness and efficiency of operations;**
- **Reliability of financial and nonfinancial reporting;**
- **Compliance with applicable laws and regulations; and**
- **Financial information systems compliance with the FMFIA and FFMIA**

## Federal Managers' Financial Integrity Act

The DLA management evaluated the system of internal control in effect during the current fiscal year according to the guidance prescribed in the GAO Green Book and OMB Circular A-123.

The evaluation of internal controls extends to every responsibility and activity undertaken by DLA and applies to program, administrative, operational controls, and financial reporting. Furthermore, the concept of reasonable assurance recognizes that: (1) the cost of internal controls should not exceed the expected benefits and (2) the benefits include reducing the risk associated with failing to achieve the stated objectives. Errors or irregularities may occur and not be detected because of inherent limitations in any system of internal control, including those limitations resulting from resource constraints, congressional restrictions, and other factors. The projection of any system evaluation to future periods is subject to risks that procedures may be inadequate because of changes in conditions or that the degree of compliance with procedures may deteriorate. Based on the preceding description, DLA is providing a statement of no assurance.

DLA considered the five components and seventeen principles defined by the GAO Green Book to conclude its determination of statement of no assurance. Based on the standards, DLA Organizations identified deficiencies and gaps in Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring. DLA lacks a robust Control Environment with adequately documented policies and procedures to help ensure DLA's Control Activities are designed, implemented, and operating effectively. The Risk Assessment component evaluates the risk the entity is facing as it seeks to achieve its objectives and provide the basis for developing appropriate risk responses. In addition, DLA has not executed a robust fraud risk management in alignment with GAO and DoD requirements. Furthermore, for the Information and Communication component DLA is still working on producing quality data; this negatively affects communication as well as the accuracy of the data represented in the agency's audited financial statements. Improvements in Monitoring are ongoing.

The consolidation of DLA Agency's Internal Control self-evaluations and a holistic assessment of pervasive DLA-wide deficiencies leads to the conclusion that DLA needs substantial improvements in its overall system of internal control. As a result, DLA is unable to support reasonable assurance that its system of internal controls is adequate to comply with the governing Federal guidance.

DLA reports all self-identified operations, reporting, and systems related Material Weaknesses (MWs) and Significant Deficiencies (SDs) along with abbreviated root cause descriptions and summaries of the Corrective Action Plans (CAPs) to remediate those deficiencies. The MWs and SDs reported by DLA contribute to the Department leadership's determination of the Agency Wide audit priorities. After submitting the Contract Administration material weaknesses for closure in FY 2023, DLA has no self-identified significant deficiencies or material weaknesses, and therefore no Material Weaknesses to remove or downgrade.

For all material weaknesses and deficiencies, including control deficiencies, DLA CAPs reflect milestones that are monitored through DLA's ERM governance forums to ensure they are met as scheduled, with minimal to no delay. As part of DLA's efforts to review and update Assessable Unit (AU) structure and Risk Appetite, DLA is undergoing a process to reevaluate the materiality of reported material weaknesses and significant deficiencies and their AU alignment/classification to ensure they merit inclusion in DLA's reporting going forward. To address the auditor-identified NFR regarding the lack of a comprehensive A-123 program, DLA developed its first RMIC Action Plan in FY 2023. This plan is designed to help define how various risk-related activities fit into a cohesive unit, in line with the DoD FY23 SOA Execution Handbook. The FY23 DLA Action Plan include: (i) RMIC program activities outlined in DLA Manual (DLAM) 5010.40, Volume 2 – Internal Control Process and (ii) expectations and timeline for DLA to achieve the SOA requirements outlined in the current year SOA Execution Handbook. As the DLA RMIC program matures each year, so too will the DLA RMIC Action Plan to include:

- A comprehensive catalog of the existing internal controls, which will have an objective of capturing and baselining the current state of DLA's Internal Control program and to support the evaluation of DLA's internal controls.

- The utilization of the existing IC inventory, reflecting the adequacy of their design and effectiveness, to communicate the current state, progress made, and issues encountered to DLA senior leaders.

- A data-driven and insight-focused database that will be incorporated into a larger reporting tool, making it easier to build a strong understanding of our internal control environment and to identify relationships between risks, internal controls, and established/necessary risk management/internal control frameworks.

The RMIC Action Plan will help DLA achieve a robust and effective Internal Control Program and favorable results when evaluating its overall IC system.

The DLA's Summary of Financial Statement Audit and Management Assurances for the SOA package and audit related material weaknesses are presented in the OI section of this report.

## Federal Financial Management Improvement Act

FFMIA was enacted to advance Federal financial management by ensuring that Federal financial management systems can routinely provide reliable financial information uniformly across the Federal government following OMB Circular A-123 Appendix D, *Management of Financial Management Systems – Risk and Compliance*. The FFMIA requires agencies to establish and maintain financial management systems that substantially comply with the following three FFMIA Section 803(a) requirements:

- Federal Financial Management System Requirements (FFMSRs)

- Federal Accounting Standards

- U.S. Standard General Ledger (USSGL) at the transaction level

OMB Circular A-123, Appendix D provides the compliance determination framework to evaluate compliance with the FFMIA requirements. The FFMIA compliance determination framework includes a series of Federal financial management goals applicable across all Federal Agencies and associated compliance indicators that assist the Agency head in determining whether the Agency has substantially complied with the requirements of FFMIA.

The DLA leveraged the OMB Circular A-123, Appendix D compliance determination framework to perform a review of data for each of the FFMIA compliance indicators and associated analysis in order to determine our current level of compliance with FFMIA and the additional actions necessary to reach full compliance. The results of the agency's analysis of relevant FFMIA compliance indicators indicate that there exist high-risk factors associated with all three FFMIA Section 803(a) requirements. The risks are described as follow:

### FFMSRs:

High-risk factors include: the disclaimer of opinion on the FY 2022 and FY 2023 financial statements; and material weaknesses reported in FY 2022 and FY 2023 in areas that corresponded to FFMSRs.

### Federal Accounting Standards[3]:

High-risk factors include: the disclaimer of opinion on the FY 2022 and FY 2023 financial statements and material weaknesses reported in FY 2022 and FY 2023 in areas that related to compliance with Federal accounting standards.

[3] Refer to the Notes to the Principal Financial Statements; Note 1.C, *Departures from U.S. GAAP.*

## USSGL at the Transaction Level:

High-risk factors include the disclaimer of opinion on the FY 2023 financial statements and material weaknesses reported in FY 2022 and FY 2023 in areas that related to implementation of the USSGL at the transaction level.

The table below summarizes the status of unresolved deficiencies associated with each of the FFMIA Section 803(a) requirements and remediation activities that are planned or underway, target dates, and offices responsible for bringing systems into compliance.

**DLA Joint Reserve Force Leaders Assemble**

During the June Battle Assembly about 65 Defense Logistics Agency Joint Reserve Force members attended the Combined Drill Weekend event June 9-11 at the McNamara Headquarters Complex, Fort Belvoir, Va. **Photo by:** Master Sgt. Scott Mathews

| FFMIA Section 803(a) Requirement | Remediation Activities | Target Date | Responsible Offices |
|---|---|---|---|
| Federal Financial Management System Requirements | The DLA will continue to develop and document policies, procedures, and controls in order to comply with standards, laws, and regulations that promote reliable financial reporting and effective and efficient operations. | FY 2024 - FY 2026 | • Finance<br>• Information Operations<br>• Acquisition<br>• Logistics Operations |
| FASAB | The DLA will continue to perform a root cause analysis to identify underlying issues as well as develop and document policies, procedures, and controls to maintain accounting data to permit reporting in accordance with U.S. GAAP as established by the FASAB. | FY 2024 - FY 2026 | • Finance<br>• Information Operations<br>• Acquisition<br>• Logistics Operations |
| USSGL at the Transaction Level | To reduce the material risks of procedural and posting logic deficiencies and achieve compliance with applicable accounting regulations, DLA will identify non-compliant areas with a financial impact in processes across the enterprise. This approach will include creating and updating policies, procedures and internal controls, as well as requesting the implementation of system changes to address underlying errors in the systemic posting logic. | FY 2024 - FY 2026 | • Finance<br>• Information Operations<br>• Acquisition<br>• Logistics Operations |

# Compliance with Laws and Regulations

## Anti-Deficiency Act

The Anti-Deficiency Act (ADA) Title 31 U.S.C. §1341, prohibits Federal employees from obligating funds in excess of an appropriation or before funds are available, or from accepting voluntary services. As required by the ADA, DLA notifies all appropriate authorities of any potential ADA violations. At this time, there are no known ADA violations for DLA WCF and GF. One potential DLA NDSTF violation (Case 23-01) was identified in September 2023. DLA will be conducting a preliminary investigation in FY 2024 related to this incident.

DLA is continuously evaluating the existing processes and controls to identify areas of improvement.

## Digital Accountability and Transparency Act of 2014

The Digital Accountability and Transparency Act of 2014 (DATA Act) expands the Federal Funding Accountability and Transparency Act of 2006 to increase accountability and transparency in Federal spending, making Federal expenditure information more accessible to the public. It directs the Federal Government to use government-wide data standards for developing and publishing reports and to make more information, including award-related data, available on USASpending.gov. The standards and data allow stakeholders to track Federal spending more effectively.

DLA is in the process of implementing an Agency-wide Data Quality Plan (DQP) in accordance with OMB Memorandum M-18-16, Appendix A to OMB Circular A-123, *Management Reporting of Data and Data Integrity Risk*, to support data quality improvement efforts and manage risks to data quality in accordance with OMB Circular A-123. As such, DLA as a component of DoD presently relies on the DoD DQP to satisfy the OMB requirement. During FY 2023, DLA continued implementation of its DQP, as well as test plans to assess controls and monitor and improve procurement data quality in the core financial system, Enterprise Business System (EBS). Furthermore, DLA WCF has identified a fund code for appropriations specific to funding for COVID-19, and the use of specific internal order numbers to track additional expenses resulting from COVID-19, in accordance with OMB Memorandum M-20-21, *Implementation Guidance for Supplemental Funding Provided in Response to the Coronavirus Disease 2019*, as implemented by Office of the Under Secretary of Defense (Comptroller) memorandum, Coronavirus Disease *2019 Disaster and Emergency Relief Accounting and Reporting Requirements*, April 9, 2020.

The DLA is unable to provide assurance over compliance with the DATA Act.

## Debt Collection Improvement Act of 1996

The Debt Collection Improvement Act of 1996 requires Federal Agencies to refer legally enforceable, past due, non-tax debts to the Secretary of the Treasury after 180 days. Section 5 of the Digital Accountability and Transparency Act of 2014 amended the Debt Collection Improvement Act of 1996 to reduce the time period to 120 days.

Accordingly, at the end of each fiscal quarter, the Defense Finance and Accounting Service (DFAS) prepares the Treasury Report on Receivables (TROR) to notify the Secretary of the Treasury of receivables due from the public aged more than 120 days.

In FY 2023, DLA has adequately reported all instances of delinquent debts over 120 days to the Secretary of Treasury in compliance with the Debt Collections Improvement Act.

## Prompt Payment Act, 31 U.S.C. §§ 3901–3907

In 1982, Congress enacted the Prompt Payment Act (PPA) to require Federal Agencies to pay their bills on a timely basis, to pay interest penalties when payments are made late, and to take discounts only when payments are made by the discount date.

The DLA is unable to provide assurance over compliance with the PPA.

## Government Charge Card Abuse Prevention Act of 2012

The Charge Card Abuse Prevention Act (Charge Card Act) requires Agencies to establish and maintain safeguards and internal controls for purchase cards, travel cards, integrated cards, and centrally billed accounts. Furthermore, the Charge Card Act requires Agencies to report purchase card violations, and the Inspector General to conduct periodic risk assessments of government charge card programs. DLA is unable to provide assurance over compliance with the Charge Card Act but has multiple layers of processes and controls in place to identify fraudulent purchases.

In order to mitigate the risk of fraud, DLA uses the DoD mandated Insight on Demand (IOD) system, which is an artificial intelligence data mining platform that automatically analyzes Government Purchase Card (GPC) data to identify and flag high risk transactions. Agency/Organization Program Coordinators (A/OPC) and Approving/Billing Officials (A/BO) review 100% of all flagged IOD data mining cases daily. A/OPCs complete a monthly checklist within IOD, which is a series of oversight questions related to appointment and training, and the Component Program Managers (CPMs) review the monthly A/OPC reports within IOD to include corrective actions taken for any identified non-compliance. A/OPCs complete a semi-annual head of activity report within IOD that captures program oversight data, including the number of transactions flagged for review, findings, and corrective actions assigned. The A/OPCs brief their head of activity with the results. CPMs complete a semi-annual head of activity report within IOD that captures program oversight data at the Agency level and briefs to the Senior Procurement Executive.

In addition to IOD, DLA has processes in place for A/BOs, A/OPCs, and the CPMs to conduct transaction reviews and overall program compliance reviews in order to mitigate the risk of fraud and misuse. MSC audit teams also conduct GPC reviews. As a result of IOD and DLA processes, transactions are reviewed by A/BOs, A/OPCs, and CPMs daily, monthly, semi-annually, and annually with corrective action assigned as appropriate.

Daily, management approves all requirements before the cardholder makes the purchase. A/BOs approve the use of the GPC as the method of payment and review 100% of purchases made by cardholders. The A/OPCs perform a monthly review over a minimum of 6.0% of all cardholder transactions, take corrective action and provide results to the CPM for review. The A/OPCs and CPMs also review all monthly statement approval and certifications to identify any A/BO violations of segregation of duty policies.

CPM also conducts an annual comprehensive program review of each DLA GPC Activity, which includes a random sampling of cardholder transactions, appointment and training documentation, and overall program oversight responsibilities. The CPM assigns corrective actions as appropriate and provides results to senior leadership.

During FY 2023, there were no instances of fraud identified as a result of reviews or audits.

**Filling a Cast**

Foundry Artisans fill mold to manufacture a casting. Stainless Foundry and Engineering, Wisconsin. March 31, 2022

**Photo By:** Nutan Chada, DLA Public Affairs

# Financial Systems

## Financial Management Systems Strategy

DLA continues to strive toward providing financial management systems that enable, support, and optimize the performance of financial activities; ensure accountability and control of resources; and produce accurate, consistent, and timely financial and program information to inform Agency decision-makers at all levels. DLA financial management systems continue to undergo profound changes essential to maintaining and optimizing operational effectiveness in support of fiscal stewardship – a DLA strategic and critical capability.

The DLA is continuously adopting modern software engineering practices to advance technology for the future mission. DLA has migrated its principal financial management system – the EBS – from a legacy to a modern cloud environment and is engaged in a major system upgrade. Harnessing modern technological practices will allow DLA to maximize readiness while increasing operational excellence.

DLA is unable to provide assurance that its financial management systems comply with relevant federal statutory and regulatory requirements including both financial accounting and system security requirements. These changes will in effect lend themselves to improve DLA's overall financial management system compliance posture by eliminating and remediating deficiencies through reengineering, thus ensuring compliance with relevant federal laws, regulations, and policies affecting financial management systems.

DLA continues to review audit findings from prior and current financial statement audits and coalesce finance and other business stakeholders to develop Corrective Action Plans (CAPs) and resolve findings. Identified deficiencies are prioritized and aligned to the appropriate plans and system enhancements.

In addition to identified audit findings, DLA is working to become compliant with DoD requirements including Standard Financial Information Structure (SFIS) and Standard Line of Accounting (SLOA). The implementation of DoD SLOA will improve interoperability between DoD business systems and provide better end-to-end funds traceability and eliminations reporting to enable successful audits in DoD. Improvements to general ledger posting logic to comply with the USSGL are also being implemented proactively to ensure all business events are mapped to the proper general ledger accounts.

Both Finance (J8) and Information Operations (J6) work collaboratively to build a roadmap for future financial management system improvements based on budget availability, resource, and system constraints. DLA's financial management systems strategy supports the overarching strategy of DLA to align end-to-end business processes with financial statements line items with a focus on risk and controls. DLA will also continue to focus on remediating any issues associated with material weaknesses and DoD Chief Financial Officer (CFO) and Chief Information Officer (CIO) priorities.

Additionally, as part of the 2021-2026 Strategic Plan, DLA's Digital-Business Transformation will continue its focus on IT and digital capability investments on key areas including effective data management, which will enable DLA to develop data and analysis as a service providing data-driven insights and solutions to DLA business users including those in the finance domain. This includes facilitating access to data from various sources such as financial systems, enabling DLA finance users to automate tasks, improve accuracy, reduce costs, and enhance decision making. DLA data and analysis as a service for finance users will also promote the use of data analytics tools and techniques that promote more predictive and data-driven decisions.

## Financial Management Systems Framework

The DLA relies on EBS as its principal financial management system of record to process, track and report all business events which impact DLA WCF, GF and NDSTF. The core of EBS is Systems Applications and Product's (SAP) ERP (Enterprise Resource Planning) Central Component (ECC) version 6.0. This is a cloud-hosted, commercial off-the-shelf (COTS) software product that has been configured and customized to meet DLA's business requirements. However, due to system deficiencies, DLA is unable to provide assurance that EBS is in compliance with Federal accounting and security requirements. There are numerous systems which interface with EBS. These include but are not limited to inventory and customer ordering systems, including the Distribution Standard System, a legacy inventory warehouse management system and multiple DFAS systems, including the Defense Departmental Reporting System (DDRS) – for the creation of financial statements, reports, and Treasury cash management. DLA EBS ECC 6.0 has a single, enterprise general ledger which is used for all funds.

## Future Financial Management Systems Framework

DLA migrated the existing EBS SAP ERP application environment to SAP's Secure HANA Cloud (SHC) platform. DLA has also begun the process for migrating its principal financial management system, EBS SAP ECC 6.0 to SAP S/4HANA in SAP's SHC. These migrations will provide an improved cyber security posture as well as enhanced capabilities for accounting and financial reporting and improved auditability.

The DLA is in the third year of a two phased ERP Migration. Phase 1 was ERP Migration to Cloud (M2C) and during this phase all applications that were within the EBS accreditation boundary were migrated to SAP's Secure HANA Cloud platform. Phase 1 was successfully completed on February 22, 2022. Phase 2, started concurrently with Phase 1, is DLA's ERP Migration to Standard (M2S) – SAP S/4HANA in SAP's SHC. Phase 2 has four sub-phases: Business Transformation Study (BTS), Business Process Reengineering (BPR), Requirements Development, and Execution. The ERP Transformation execution contract is planned to be awarded on April 1, 2024, with a planned final implementation date (Go Live) of September 29, 2027.

The DLA Business Transformation Study (BTS) – completed in FY 2022, identified opportunities for business processes reengineering – opportunities to de-customize and adopt standard SAP S/4 HANA capability. DLA is currently conducting BPR with the goal of eliminating as much customization as possible. And thus, use standard capability to the maximum extent possible to streamline business processes, adopt industry best practices, reduce cost, and allow for better innovation going forward. DLA BPR workshops began in January 2023 and are scheduled to be completed by December 2023. BPR workshops will continue after December 2023. Working with the Integration Council, additional BPRs will be prioritized, scheduled, and put on contract starting January 2024.

The DLA will also be implementing system changes to meet the requirements of Treasury's G-Invoicing system. G-Invoicing will help address government-wide accounting elimination problems by ensuring trading partners have the same information for intragovernmental transactions. The G-Invoicing mandated implementation deadline was October 2022 for Federal Program Agencies (FPAs) for new orders with a period of performance beginning October 1, 2022, or later. FPAs must transact all Buy/Sell activity through G-Invoicing by October 2025. Currently, DLA's G-Invoicing system solution is on track for production by April 2024.


**Helping Hand**

Army Sgt. Patrick O'Hara delivers water in Sanibel Island, Fla., Oct. 1, 2022, during Hurricane Ian relief efforts. **Photo By:** Army Pfc. Alexander Helman

# Forward-Looking Information

The following areas present insights into how the Agency shapes its programs and responds to challenges posed to DLA's goals and missions.

## An Ever-Changing Workforce

The DLA is a high-performing organization, and DLA's workforce is its greatest asset. We must attract, develop, and retain a diverse, skilled and agile workforce. The two People and Culture objectives are the strategies that will assist DLA in mitigating several significant external factors that will affect DLA and its workforce.

Changing demographics are the first significant external factor. There are different generations working side-by-side in the DLA workplace and DLA civilians are playing an increasingly critical role in supporting global DoD missions. These changing demographics will require continued assessment of DLA's current human resource initiatives and new strategies to excel in areas such as recruitment, training and development, work-life balance, managing in a geographically dispersed environment while maintaining strong connections to DLA culture, knowledge transfer, leadership skills, labor management relations and a culture that fosters diversity, equity, inclusion, accessibility, and employee engagement.

Our economy is the second external factor that influences the Federal government's ability to recruit top talent and retain its workforce. It is critical that DLA not only recruits and retains a diverse workforce, but also ensures the workforce has the critical skills necessary to operate in this constrained environment.

Technology is the third external factor. Advancement of self-service capabilities, easy access to people and tools that employees need, and automation of routine process are in DLA's future. In partnership with DLA Information Operations (J6), DLA Human Resources (J1) is currently working on expanding their technological footprint with the use of ServiceNow. Through the use of ServiceNow, the self-service capabilities for employees will expand to a new level. Employees will be able to use a single point of entry to gain access to all things J1. Employees will immediately be sent to the correct point of contact based on their need, they will be able to submit requests through a monitored tracking system, where employee can check status at any time, engage with chat bots on routine questions, and get the HR related forms they need at any time. J1 and J6 have started the process for implementation with the first phase being pushed out by end of Fiscal Year 2024.

The work environment is the last significant external factor to impact DLA's workforce. DLA's success as an organization is largely dependent on DLA's ability to achieve a high-performing, results-driven culture and to sustain that culture in light of changes to demographics, economics, and technology. These factors will impact each segment of DLA, and DLA Human Resources must strategically partner with leadership and the workforce to carry out DLA's mission. The use of change management techniques will assist in decreasing the uncertainty associated with changes as well as mitigate resistance to those changes.

The DLA has a critical mission to support the Military Services, Combatant Commands, and other Federal Agencies; that includes supporting our Nation's response to COVID-19. As of May 11, 2023, the Coronavirus national and public health emergency expired. The Consolidated Department of Defense Coronavirus Disease 2019 Force Health Protection Guidance – Revision 4, as of January 30, 2023 issued by the Under Secretary of Defense for Personnel and Readiness presents a uniform and consolidated DoD policy for the Department's response to the COVID-19 pandemic. As an employer, DLA will continue to follow DoD policies and guidelines in taking any actions to address the COVID-19 Reentry and Safety Plan.

DLA leaders are committed to protecting our workforce from the effects of the COVID-19 pandemic while preserving the Agency's ability to be mission ready. As DoD revises and develops new policies to protect the workforce, the DLA CCT will continue to provide implementation guidance as appropriate for DLA worksites. Each DLA major population center has its own plan for returning employees to the workplace, all based on common guidance for a condition- based, deliberate, and safe return. Different locations will go through the various phases on different timelines accounting for local conditions. DLA is monitoring workforce availability and conducting site capability and capacity assessments. DLA will continue to encourage completion of COVID-19 worksite related trainings and to develop methods to effectively hire and onboard personnel with a plan for virtual training and orientation.

## External Threats

In response to the President's call for governmental reform and under the Direction of the Chief Management Officer, DoD is reviewing, changing, and setting up processes, where appropriate, to gain efficiencies and maximize savings to reinvest into service readiness. This is aligned to the LOE of Warfighter Always.

The DoD as a whole faces numerous challenges – ranging from strategic competition and aggression from other nations and the threat of terrorism to the concern of securing funding necessary to accomplish the mission. These threats directly affect DLA's mission and goals. As the Nation's Combat Logistics Support Agency, DLA monitors these external threats to ensure readiness and support of the Warfighter.

In addition, DLA continuously reviews its strategy to meet global mission requirements as prescribed by DoD. DLA conducted a review of our current strategy against the FY 2023 NDAA DoD Strategic Management Plan (SMP) for Fiscal Years 2022 – 2026, the 2023 ASD(S) Strategic Plan and supporting metrics, DoDI 3000.LU, "Strategic Readiness" policy, and A&S Big Plays Memo to assess their impact and ensure alignment with DLA's 2021-2026 Strategic Plan remains in effect. DLA assisted ASD(S) to rename their Goal 4 to "Optimize Warfighter Logistics" and descoping the three supporting objectives to areas that DLA can impact/influence within the ASD(S) Strategic Plan. DLA was also part of the FY 2023- 2024 Defense Activity Field Activity (DAFA) Review. Section 192(c) of Title 10, U.S.C. directs the Secretary of Defense to review the efficiency and effectiveness of each DAFA, and this cycle included three specific focus areas for DLA: contingency demand planning, depot-level reparables, and warehouse utilization. After completion of the review, the Director of Administration & Management (DA&M) will provide a consolidated report on the review to the congressional defense committees. The report is expected to be completed in 2nd Quarter FY 2024 and will include the information required by law, together with any additional information deemed necessary and appropriate by the DA&M. Our Strategic Plan is designed to meet the evolving requirements of the Warfighter and the nation with a targeted transformative approach encompassing the most critical priorities for the next four years. DLA's Strategic Plan reaffirms and extends DLA's commitment to Warfighter readiness and lethality and to self- accountability. The plan describes five LOEs and three CCs that DLA leverages to provide global, end-to-end supply chain solutions: Warfighter Always, Support to the Nation, Trusted Mission Partner, Modernized Acquisition and Supply Chain Management, Future of Work, People and Culture, Fiscal Stewardship, and Digital-Business Transformation. Each LOE or CC has specific objectives.

Within the context of external threats to economic stability, national security, and Warfighter readiness, DLA's Enterprise Risk Management (ERM) program proactively takes a strategically aligned, risk-based approach to protecting our ability to achieve stated mission goals and objectives. Leveraging ERM as a strategic capability, DLA is continuing to mature its ability to identify the threats and opportunities associated with uncertainty and to build priority-based, data driven responses that appropriately align with DLA's Risk Appetite and Risk Tolerance levels.

ERM takes an integrated, strategic approach to supporting DLA's mission while managing risks by providing a prioritized listing of agency-wide risks in an annual Risk Profile. Employing a rigorous approach, DLA coordinates across the enterprise to establish the annual Risk Profile as part of the Statement of Assurance deliverables DLA transmits to OUSD(C) annually. In FY 2023, DLA executed a comprehensive "top down" and "bottom up" approach to identifying, assessing, consolidating, and prioritizing DLA's enterprise-level risks. Upon thorough discussion amongst senior leadership within established ERM governance forums, DLA affirmed its commitment to protecting DLA's operational resiliency and strategic priorities through its approved FY 2023 DLA Risk Profile. The items identified all represent potential threats to DLA's ability to achieve its strategic objectives and support the Warfighter if the risks are realized. Risks identified in FY 2023's Risk Profile are:

- Supply Chain Security
- Industrial Base Vulnerabilities
- Achieving Readiness Objectives while Maintaining Fiscal Solvency and Affordability
- Loss of Critical Technology Capability
- Audit Opinion Progress

The DLA faces current and future cyber threats that must be countered in a sustained effort to secure and defend the Agency's critical operational data, network, and business systems by applying key security principles, which include:

Continued on next page ►

- Operations-level situational awareness;
- Layered perimeter defenses;
- Least privilege for access to data and IT capabilities; and
- Physical or logical segmentation of networks, services, and applications.

The DLA continues to provide limited support to the U.S. response to COVID-19 in the areas of material support, planning, and acquisition as COVID-19 response initiatives reduce levels of effort.

DLA efforts relating to climate risks are reported at the DoD wide level, as instructed per OMB Circular A-136 requirements for Significant Entities and the Treasury Financial Manual (TFM), Volume 1, Part 2, Chapter 4700, Appendix 1a, *List of Significant Entities*. The DoD sustainability and adaptation plans, reports, and scorecards can be found at: Federal Progress, Plans, and Performance | Office of the Federal Chief Sustainability Officer.

## Technological Advancement and Initiatives

Digital-Business Transformation (D-BX) is a value-driven Critical Capability in DLA's 2021-2026 Strategic Plan. It focuses on a collaborative effort between the business and Information Operations to invest in digital modernization, which will enable DLA to enhance performance, reduce costs, make more predictive and data-driven decisions and improve customer experience. This will transform systems and processes to improve transparency, reliability, and security for DLA's employees, customers, and suppliers. DLA data assets include supply chain, acquisition, personnel, information management, and financial data, along with the infrastructure and exchanges that move it. Looking forward, effective data management will enable DLA to develop data and analysis as a service for its business users which will enable them to access it and make data-driven decisions.

New and modernized technology is the foundation of D-BX, and DLA Information Operations continuously evaluates the IT operating environment to identify opportunities to streamline and automate processes and ensure alignment with DoD and DLA Strategic Initiatives. One example of these types of efforts in process includes increasing the use of cloud computing technologies and solutions. Many applications have initiated cloud computing migration.

Finally, DLA GF provides Congressionally appropriated funding to other Defense Organizations for the development of the Defense Agencies Initiative (DAI). The DAI mission is to deliver auditable, CFO Act compliant business environments for Defense Agencies. The goal is to provide accurate, timely, and authoritative financial data in support of DoD goals to standardize financial management practices, improve financial decision support, and enhance audit readiness. DAI is a critical DoD effort to modernize the Defense Agencies' financial management capabilities.

**Building Buddies**
Airmen put up tents during an operational readiness exercise at Andersen Air Force Base, Guam, Sept. 12, 2022. **Photo By:** Air Force Airman 1st Class Lauren Clevenger

## Reflective Climb

Air Force Airman 1st Class Dylan Prusso climbs up an A-10C Thunderbolt II during Green Flag-West 23-02 at Marine Corps Air Station Miramar, Calif., Nov. 9, 2022 **Photo By:** Air Force Senior Airman Zachary Rufus

# Section 2

## *Financial Section*

(Unaudited)

◀ **Ukibaru View**

Air Force Staff Sgt. Jordan Cate participates in a search and rescue exercise off the coast of Ukibaru Island, Japan, Jan. 19, 2023.

**Photo By:** Air Force 1st Lt. Robert Dabbs

# Section 2

## ***Financial Section*** (Unaudited)

### In this section:

*November 2023*

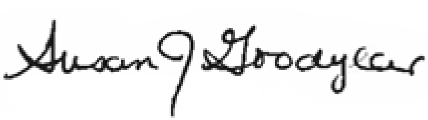
# Message from the Chief Financial Officer

I am proud to join the Director in issuing our Fiscal Year (FY) 2023 Agency Financial Report (AFR), the sixth Defense Logistics Agency (DLA) has issued since an Independent Public Accounting firm commenced the financial statement audit of the Working Capital Fund (WCF), General Fund (GF), and National Defense Stockpile Transaction Fund (NDSTF). The FY 2023 DLA WCF, GF, and NDSTF AFR highlights valuable insights into the overall financial operations, accomplishments, and challenges of the Agency. This section of the AFR provides a comprehensive view of DLA WCF, GF, and NDSTF financial activities. DLA remains committed to providing services and ensuring value, efficiency, and effectiveness, as well as ensuring outstanding stewardship to protect against fraud, waste, and abuse in every program we manage.

Although DLA received a Disclaimer of Opinion on the Agency's WCF, GF, and NDSTF financial statements, which denotes that the auditor conducted audit procedures but was unable to express an opinion on the financial statements, DLA continues to make tremendous strides. DLA's continued efforts across all levels of the enterprise consist of establishing the framework to correct material weaknesses by reviewing, establishing, and re-engineering end-to-end business processes, evaluating operational impacts on the financial statements, identifying the financial statement and financial reporting risks, and designing and implementing the appropriate controls to address those risks.

The DLA enterprise efforts include initiatives to improve financial operations (budgeting, accounting, and reporting) to enhance the value provided to the Warfighter and our partners. DLA continues to focus efforts and resources towards upgrading financial and operational systems, remediating audit findings in areas with the greatest impact to readiness and lethality, while improving financial data and internal controls to achieve an unmodified audit opinion.

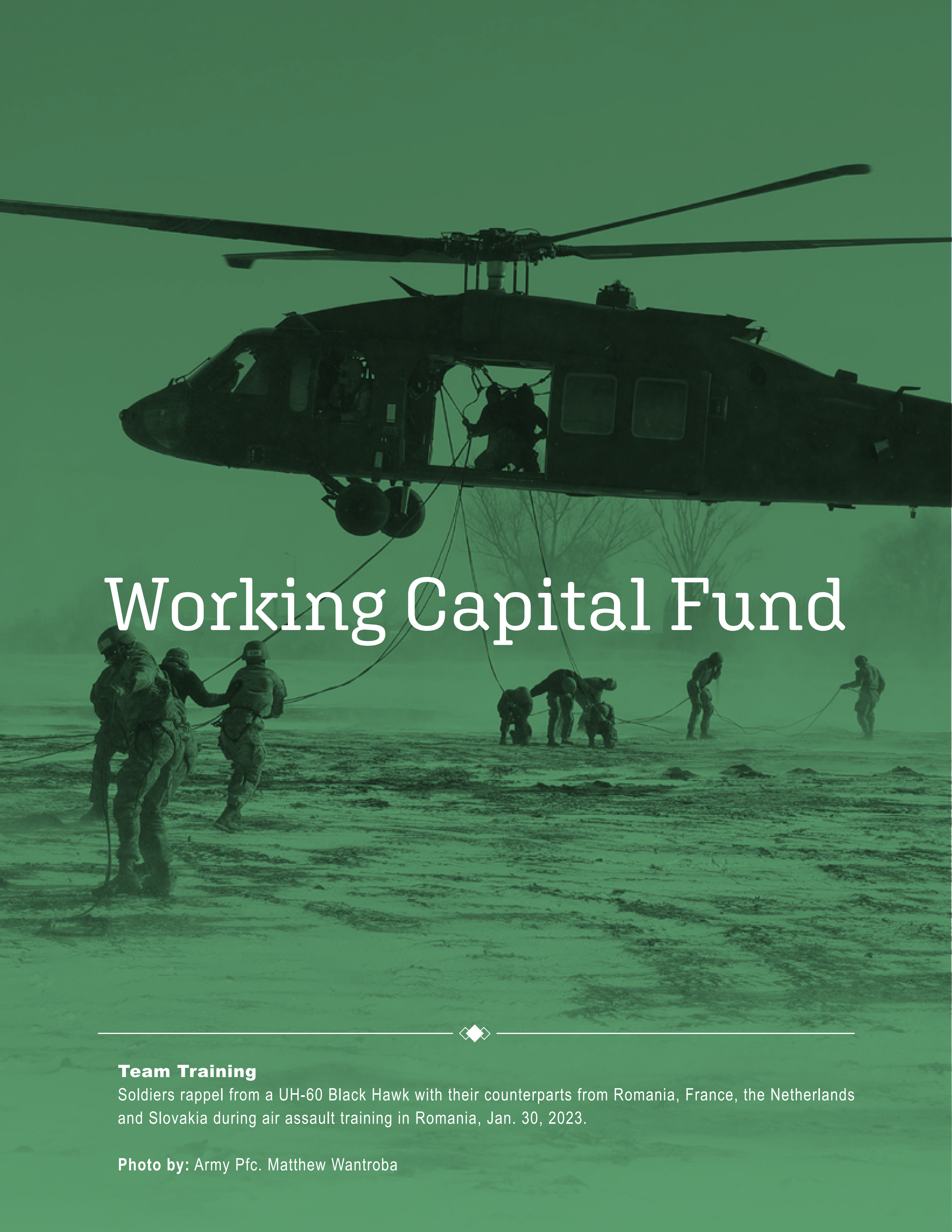
As DLA continues to evolve in the audit process, we will continue to learn and use that knowledge to improve, reform and protect our business operations and financial processes, allowing us to maximize our resources in support of the Warfighter. One of our highest priorities is to provide enhanced financial management and strong governance in support of our goals to identify and address risks, successfully manage challenges, and implement actions to remediate material weaknesses. Our commitment to fiscal stewardship is paramount in supporting the Warfighter and demonstrates prudent use of the American taxpayer funds entrusted to us.



SUSAN GOODYEAR
DIRECTOR, DLA FINANCE
**CHIEF FINANCIAL OFFICER**

## WARFIGHTERS ALWAYS

# Working Capital Fund



**Team Training**
Soldiers rappel from a UH-60 Black Hawk with their counterparts from Romania, France, the Netherlands and Slovakia during air assault training in Romania, Jan. 30, 2023.

**Photo by:** Army Pfc. Matthew Wantroba

# Audit Reports

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

November 8, 2023

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)/
CHIEF FINANCIAL OFFICER, DOD
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Transmittal of the Independent Auditor's Reports on the Defense Logistics Agency Working Capital Fund Financial Statements and Related Notes for FY 2023 and FY 2022
(Project No. D2023-D000FE-0048.000, Report No. DODIG-2024-018)

We contracted with the independent public accounting firm of Ernst & Young, LLP (EY) to audit the Defense Logistics Agency (DLA) Working Capital Fund Financial Statements and related notes as of and for the fiscal years ended September 30, 2023, and 2022. The contract required EY to provide a report on internal control over financial reporting and compliance with provisions of applicable laws and regulations, contracts, and grant agreements, and to report on whether the DLA's financial management systems substantially complied with the requirements of the Federal Financial Management Improvement Act of 1996. The contract required EY to conduct the audit in accordance with generally accepted government auditing standards (GAGAS); Office of Management and Budget audit guidance; and the Government Accountability Office/Council of the Inspectors General on Integrity and Efficiency, "Financial Audit Manual," Volume 1, May 2023, Volume 2, May 2023, and Volume 3, June 2023. EY's Independent Auditor's Reports are attached.

EY's audit resulted in a disclaimer of opinion. EY could not obtain sufficient, appropriate audit evidence to support the reported amounts within the DLA Working Capital Fund Financial Statements. As a result, EY could not conclude whether the financial statements and related notes were presented fairly and in accordance with Generally Accepted Accounting Principles. Accordingly, EY did not express an opinion on the DLA Working Capital Fund FY 2023 and FY 2022 Financial Statements and related notes.

EY's separate report, "Report of Independent Auditors on Internal Control Over Financial Reporting," discusses seven material weaknesses related to the DLA's internal controls over financial reporting.* Specifically, EY's report stated that the DLA did not:

- validate and support Inventory balances and transactions;
- reconcile Fund Balance with Treasury;
- record Accounts Receivable and revenue transactions properly;
- support Accounts Payable, expenses, and related budgetary balances;
- design controls over the financial statement reporting process to identify and prevent inaccurate balances and footnotes;
- document end-to-end business processes, monitor internal control risks, and remediate audit findings; or
- ensure the effective design and operation of financial reporting information systems.

EY's additional report, "Report of Independent Auditors on Compliance and Other Matters," discusses two instances of noncompliance with provisions of applicable laws and regulations, contracts, and grant agreements. Specifically, EY's report describes instances in which the DLA's financial management systems did not comply with the Federal Financial Management Improvement Act of 1996 and the Federal Managers' Financial Integrity Act of 1982.

In connection with the contract, we reviewed EY's reports and related documentation and discussed them with EY's representatives. Our review, as differentiated from an audit of the financial statements and related notes in accordance with GAGAS, was not intended to enable us to express, and we do not express, an opinion on the DLA Working Capital Fund FY 2023 and FY 2022 Financial Statements and related notes. Furthermore, we do not express conclusions on the effectiveness of internal controls over financial reporting, on whether the DLA's financial systems substantially complied with Federal Financial Management Improvement Act of 1996 requirements, or on compliance with provisions of applicable laws and regulations, contracts, and grant agreements. Our review disclosed no instances where EY did not comply, in all material

* A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting that results in a reasonable possibility that management will not prevent, or detect and correct, a material misstatement in the financial statements in a timely manner.

respects, with GAGAS. EY is responsible for the attached November 8, 2023 reports and the conclusions expressed within the reports.

We appreciate the cooperation and assistance received during the audit. If you have any questions, please contact me.

FOR THE INSPECTOR GENERAL:

Lorin T. Venable

Lorin T. Venable, CPA
Assistant Inspector General for Audit
Financial Management and Reporting

Attachments:
As stated

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# Report of Independent Auditors

The Director of the Defense Logistics Agency and the
Inspector General of the Department of Defense

## Report on the Audit of the Financial Statements

### *Disclaimer of Opinion*

We were engaged to audit the financial statements of the Working Capital Fund (WCF) of the Defense Logistics Agency (DLA), which comprise the balance sheets as of September 30, 2023 and 2022, and the related statements of net cost and changes in net position and combined statements of budgetary resources for the years then ended, and the related notes (collectively referred to as the "financial statements").

We do not express an opinion on the accompanying financial statements of DLA. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

### *Basis for Disclaimer of Opinion*

DLA continues to have unresolved accounting issues and material weaknesses in internal controls that cause DLA to be unable to provide sufficient evidential support for complete and accurate financial statements on a timely basis. As a result of these matters, we were unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded balances and the elements making up DLA's financial statements as of and for the years ended September 30, 2023 and 2022.

### *Departures from U.S. Generally Accepted Accounting Principles*

As described in Note 1, DLA has not implemented certain accounting standards for the Department of Defense and the federal government. The effect of these matters on DLA's financial statements as of and for the years ended September 30, 2023 and 2022 is not currently determinable by DLA and could be material.

### *Responsibilities of Management for the Financial Statements*

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and

fair presentation of the financial statements that are free of material misstatement, whether due to fraud or error.

***Auditor's Responsibilities for the Audit of the Financial Statements***

Our responsibility is to conduct an audit of DLA's financial statements in accordance with auditing standards generally accepted in the United States of America, in accordance with the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States (*Government Auditing Standards*), and in accordance with the provisions of Office of Management and Budget Bulletin No. 24-01, *Audit Requirements for Federal Financial Statements*, and to issue an auditor's report. However, because of the matters described in the Basis for Disclaimer of Opinion section of our report, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

We are required to be independent of DLA and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audit.

***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Required Supplementary Information, as listed in the Table of Contents, be presented to supplement the financial statements. Such information is the responsibility of management and, although not a part of the financial statements, is required by the Federal Accounting Standards Advisory Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We were unable to apply certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report. We do not express an opinion or provide any assurance on the information.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we also have issued our reports dated November 8, 2023, on our consideration of DLA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of those reports is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of DLA's internal control over financial

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reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DLA's internal control over financial reporting and compliance.

Ernst & Young LLP

November 8, 2023

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# Report of Independent Auditors on Internal Control Over Financial Reporting Based on an Engagement to Audit the Financial Statements Performed in Accordance with *Government Auditing Standards*

The Director of the Defense Logistics Agency and the
Inspector General of the Department of Defense

We were engaged to audit, in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States (*Government Auditing Standards)* and the provisions of Office of Management and Budget (OMB) Bulletin No. 24-01, *Audit Requirements for Federal Financial Statements*, the financial statements of the Working Capital Fund of the Defense Logistics Agency (DLA), which comprise the balance sheet as of September 30, 2023, and the related statements of net cost, and changes in net position and combined statement of budgetary resources for the year then ended, and the related notes (collectively referred to as the "financial statements"), and have issued our report thereon dated November 8, 2023. Our report disclaims an opinion on the financial statements because DLA continues to have unresolved accounting issues and material weaknesses in internal controls that cause DLA to be unable to provide sufficient evidential support for complete and accurate financial statements on a timely basis.

**Report on Internal Control Over Financial Reporting**

In connection with our engagement to audit the financial statements, we considered DLA's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of DLA's internal control. Accordingly, we do not express an opinion on the effectiveness of DLA's internal control. We did not consider all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA), such as those controls relevant to preparing performance information ensuring efficient operations.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as described below and in more detail in Appendix A, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiencies described below and in Appendix A as items I through VII to be material weaknesses.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described below and in Appendix B as items I and II to be significant deficiencies.

**Material Weaknesses**

We identified the following matters involving internal control over financial reporting and its operation that we consider to be material weaknesses, as defined above:

I. Inventory – Inventory is comprised of items held by DLA for resale. DLA also holds inventory items on behalf of the military services. Policies, procedures and internal controls surrounding documentation of procurements, shipments, and other movements, tracking of inventory by owner, validating the perpetual inventory systems by performing periodic physical counts, accumulating cost of inventory and supporting inventory balances and transactions all had deficiencies. The combination of these deficiencies in aggregate results in a material weakness in internal control related to inventory. The matters identified related to inventory are further described in Appendix A.

II. Fund Balance with Treasury (FBwT) – FBwT represents the aggregate amount of funds in DLA's account with U.S. Treasury. DLA was unable to reconcile the FBwT ending balances from the general ledger directly to the U.S. Treasury. Furthermore, DLA was unable to provide detailed listings of collections and disbursements that reconcile to the general ledger. DLA, in conjunction with Defense Finance and Accounting Services (DFAS), has implemented the Cash Management Reconciliation (CMR) and Department 97 Report Reconciliation Tool (DRRT) processes as mechanisms to reconcile DLA's general ledger to U.S. Treasury. However, these tools had known control deficiencies and reconciling issues. In addition, DLA did not have sufficient policies, procedures and internal controls in place for the end-to-end FBwT process. The combination of these deficiencies in aggregate results in a material weakness in internal control related to FBwT. The matters identified related to FBwT are further described in Appendix A.

III. Accounts Receivable (AR) and Revenue – AR consists of amounts owed to DLA primarily related to the resale of goods and the provision of services. Revenue is earned when DLA sells goods and services to the public or other federal entities. DLA was unable to support the balances recorded as AR and validate the significant balance of aged receivables and unfilled customer orders. In addition, DLA did not have procedures to estimate valuation allowances against receivables and had not supported transactions recorded. Furthermore, DLA did not have adequate policies, procedures and controls to record AR and revenue transactions accurately and in the proper period in accordance with U.S. generally accepted accounting principles (GAAP). The combination of these deficiencies in aggregate results in a material weakness in internal control related to AR and revenue. The matters identified related to AR and revenue are further described in Appendix A.

IV. Accounts Payable (AP) and Expense – AP represents the amount owed to third parties by DLA for goods and services received. Expenses are incurred and recognized when DLA receives goods and services from the public or other federal entities. DLA was unable to support the AP balance, expenses and related budgetary balances. In addition, DLA did not have overall policies, procedures and internal controls for the procure to pay process, including the process to create and approve obligations and the process to review, record and pay invoices. Furthermore, DLA lacked adequate procedures to record obligations and accrue for liabilities incurred but not paid; to review and close invalid obligations; and it recorded transactions in the procure to pay process in incorrect periods. The combination of these deficiencies in aggregate results in a material weakness in internal control related to AP and expense. The matters identified related to AP and expense are further described in Appendix A.

V. Financial Reporting – Financial reporting encompasses all aspects of operations affecting DLA's ability to produce reliable financial statements and disclosures in accordance with U.S. generally accepted accounting principles GAAP. DLA's financial statement preparation process lacked sufficient controls to review and identify inaccurate balances within the financial statements and incomplete and inaccurate footnote disclosures. DLA lacked policies and procedures to validate account balances and monitor reporting variances between source systems, resulting in DLA recording unsupported journal vouchers (JVs) to correct the variances. In addition, DLA did not have controls to review and approve transactions recorded with elevated access privileges. Furthermore, DLA was unable to provide detailed listings for budgetary accounts that reconcile to the general ledger. The combination of these deficiencies in aggregate results in a material weakness in internal control related to financial reporting. The matters identified related to financial reporting are further described in Appendix A.

VI. Oversight and Monitoring – Oversight and monitoring relate to DLA's lack of establishment and implementation of a sufficient enterprise-wide control environment as required by OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management Internal Control*. DLA did not have an effective OMB Circular A-123 program, which impacted DLA's ability to appropriately identify and address significant risks for all key business processes. DLA did not implement appropriate internal controls, including the documentation of policies and procedures that describe DLA's environment related to end-to-end business processes, monitoring of service providers, related parties, systems, risks, controls and remediation of audit findings. In addition, DLA did not perform proper review of data/reports used in the execution of key controls. The combination of these deficiencies in aggregate results in a material weakness in internal control related to oversight and monitoring. The matters identified related to oversight and monitoring are further described in Appendix A.

VII. Information Systems – Our assessment of DLA's information technology (IT) controls and the computing environment identified deficiencies which, collectively, constitute a material weakness in the design and operation of information systems controls over financial data. Based on our review, we have identified five areas of deficiency which, when aggregated, result in a material weakness. The deficiencies relate to the following five areas:

- Access controls
- Configuration management
- Segregation of duties controls
- Security management/governance over implementation of security controls
- IT Operations

The matters identified related to information systems are further described in Appendix A.

**Significant Deficiencies**

We identified the following matters involving internal control over financial reporting and its operation that we consider to be significant deficiencies, as defined above:

I. Property, Plant and Equipment (PP&E) – PP&E includes general equipment, internal use software and construction-in-progress. DLA did not complete an analysis of the existence and completeness of PP&E assets or their process to value PP&E beginning balances and had weaknesses in the processes of maintaining and reconciling PP&E records. In addition, DLA did not have sufficient policies to account for leasing arrangements and whether the leasing arrangements should be accounted for as a capital or operating lease. Therefore, DLA was unable to support the existence, completeness, rights and obligations, or valuation of its PP&E. The matters identified related to PP&E are further described in Appendix B.

II. Environmental Liabilities (EL) – ELs are comprised of cleanup costs associated with the restoration of sites on real property that DLA manages. DLA lacked adequate controls to evaluate the completeness and measurement of the ELs and the ELs recorded in the financial statements. The matters identified related to EL are further described in Appendix B.

***DLA's Response to Findings***

*Government Auditing Standards* require the auditor to perform limited procedures on DLA's response to the findings identified in our engagement to audit and described in the accompanying Management's Response to Audit Reports dated November 8, 2023. DLA's response was not subjected to the other auditing procedures applied in the engagement to audit the financial statements and, accordingly, we express no opinion on the response.

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***Purpose of This Report***

The purpose of this report is solely to describe the scope of our testing of internal control and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control. This report is an integral part of an engagement to perform an audit in accordance with *Government Auditing Standards* in considering the entity's internal control. Accordingly, this communication is not suitable for any other purpose.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2023 on our tests of DLA's compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DLA's compliance.

Ernst + Young LLP

November 8, 2023

A member firm of Ernst & Young Global Limited

## Appendix A – Material Weaknesses

### I. Inventory

DLA's inventory is comprised of petroleum and aerospace products, weapon system repair parts, food, clothing and medical supplies. Inventory also includes material from the military services designated for disposal or reutilization. In accordance with FMFIA, management is responsible for establishing effective controls over and accountability for all assets for which the agency is responsible. DLA's controls and processes did not exist or was not operating in several significant areas, specifically:

A. **Lack of or Inadequate Documentation of Inventory Accounting Policies, Procedures and Controls.** DLA did not document the processes related to the significant business activities for acquisition, movement, warehousing and disposition of inventory; the related risks for each business activity; and the control activities designed to mitigate risks of material misstatement in the financial statements. The documentation lacked an accurate description of the following: financial reporting, records management, physical count policies, accounting for third-party managed inventory, the Inventory Reconciliation Framework (IRF) and various other business processes.

B. **Lack of or Inadequate Documentation to Substantiate Inventory and Inventory-Related Transactions.** DLA was unable to provide documentation that inventory balances exist, or inventory transactions occurred and were accurately recorded in the financial statements. Specifically, documentation was not available to support:
   - The completeness and accuracy of transactions recorded or the existence of balances in the general ledger and the accountable property system of record (APSR).
   - Shipping terms for sales transactions to evidence when the title and risk of loss are transferred to the buyer.
   - Balances recorded in the inventory detail reports from the financial reporting system that do not reconcile to the site-specific end-of-month reports and component financial statements.
   - Balances of fuel inventory held in pipelines or in-transit.
   - Posting of transactions in the general ledger resulting from financial events (i.e., sales, purchases, gains and losses, including gains and losses resulting from physical inventory counts).

C. **Lack of or Inadequate Policies, Procedures and Controls Over Inventory Processes**. DLA lacked or did not have adequate policies, procedures and controls, including the design of controls, over the following:
   - **Inadequately Designed Controls Over Inventory Processes.** For controls that have been implemented over significant Energy and Distribution processes, the controls were not designed to align with DLA policies or were not executed consistently. In addition, sufficient documentation did not exist to evidence the performance of the control activities.
   - **Inventory Held for Others.** Inventory held on behalf of the military services was not always stored in physically segregated locations and instead, was commingled with similar

inventory that could be owned by multiple owners. DLA lacked controls over the commingled inventory. DLA did not have policies and procedures to reconcile quantities of inventory by owner to the total physical inventory counts on a regular basis or to account for inventory variances resulting from physical inventory counts for segregated inventory items with multiple owners. As a result, gain/loss adjustments were not assigned to the appropriate owner.

- **In-Transit and Pipeline Inventory (In-Transit).** In-transit inventory relates to items that are accepted at the point of origin (free on board shipping point) and are in-transit to a DLA destination. Controls related to monitoring and reconciling in-transit inventory balances did not exist. As a result, inventory recorded as in-transit from procurement points of origin remained in-transit for several fiscal years, including amounts dating back to 2012.
- **Energy Inventory.** DLA policy requires that monthly or quarterly automated tank gauging (ATG) verifications be performed. In addition, DLA requires that manual readings of fuel tank levels be obtained by calibrated tape or calibrated rod in the absence of functional ATG systems. However, DLA lacked controls to monitor field-level sites for compliance with DLA Energy policies. In addition, DLA did not monitor or review documentation to validate that field-level sites were performing the monthly or quarterly verifications or that manual readings were obtained in the absence of functional ATG systems.
- **Posting Inventory Adjustments in the General Ledger.** DLA policy requires that errors between the APSR and the general ledger be reviewed and corrected by assigned users. Adjustments to correct the errors above a certain dollar threshold are reviewed by a supervisor. However, DLA did not have controls in place to prevent users from posting adjustments above the threshold or to detect that adjustments posted above the threshold were not reviewed.
- **Inventory Recorded in the Appropriate Period.** DLA did not have policies and procedures in place to record transactions in the period that the transaction occurred or to accrue for transactions that occurred but were not posted at period-end.

D. **Inadequate Policies, Procedures and Related Controls Over Inventory Physical Counts**. The Department of Defense Financial Management Regulation (DoD FMR) requires that all inventory be counted at least annually, either in a full physical count or through cycle counts, to validate perpetual inventory accuracy. DLA did not adequately design controls related to physical counts of inventory related to Supply or Disposition as required. For example:

- **Supply Inventory.** DLA policy requires an annual physical count of all items on hand as of the beginning balance sheet date. DLA was not in compliance with this policy or the DoD FMR. Additionally, the policies and procedures over inventory counts were not designed to adequately demonstrate that inventory counts are complete and accurate.
- **Disposition Inventory.** Inventory physical counts are not required to be performed on all Disposition inventory received from the military services.

E. **Lack of Controls for the Reconciliation Between Inventory APSR and the General Ledger.** DLA utilizes the IRF to reconcile the inventory quantity balance in the general ledger to the inventory quantity balance in the APSRs. However, the IRF was not performed completely, accurately or timely. For example:
   - The inventory reconciliations were not completed on a timely basis or within the normal financial statement close period (approximately 40-45 days from month-end).
   - There were significant unreconciled variances totaling $278 million in the reconciliation for June 2023.
   - The IRF did not include all appropriate general ledger accounts, including inventory in-transit between storage locations and inventories/stock on hand.

F. **Lack of Controls over Inventory Held by Third Parties.** DLA did not have a detailed listing of inventory by vendor that reconciles to the inventory recorded in DLA's general ledger, nor did DLA have a listing of all vendors who hold inventory on DLA's behalf. DLA was unable to support the balances of inventory held at third parties for each vendor. As a result, DLA was unable to substantiate the existence and completeness of inventory held at third parties.

G. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** DLA did not have policies, procedures and controls to effectively implement accounting standards, causing an inaccurate presentation of inventory on the balance sheet and in the related footnote disclosure. Specifically, DLA neither implemented nor applied the costing and valuation methodologies set forth by Statement of Federal Financial Accounting Standards (SFFAS) No. 3, *Accounting for Inventory and Related Property*, and SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials.* For example:
   - DLA values inventory using the moving average price (MAP). However, DLA was unable to provide supporting documentation of costs that are included or excluded to calculate the MAP.
   - DLA began implementing inventory costing methodologies in accordance with SFFAS No. 48 in fiscal year (FY) 2016. However, DLA did not completely and accurately value inventory in accordance with SFFAS No. 48. For example, the values assigned for certain inventory items were based on the latest acquisition cost (LAC). The LAC values did not properly consider inventory acquired through the implementation date.
   - DLA assigned zero-dollar values to unique material numbers and was not able to provide the basis for the zero-dollar valuation for all materials.
   - Work in process (WIP) inventory items or components are provided to a production facility for kitting, assembly or modification, or to make an end item. Policies and procedures were not in place to record all costs, such as the assembly and labor costs, incurred during the kitting, assembly or modification process.
   - Valuation allowances for various inventory items, including excess, obsolete and unserviceable (EOU) inventory, inventory held for repair, inventory held at net realizable value, etc., were not appropriately documented or supported. The documentation for the valuation allowance for inventory held for repair did not sufficiently describe the

methodology used to estimate the allowance or describe the rationale for adopting the methodology being used and the factors used in the estimation process.

H. **Inadequate or Lack of Controls Over Financial Reporting of Inventory.** DLA lacked controls to classify and present inventory appropriately in the financial statements. DLA accounting policy states that inventory balances are based on the following categories: inventory held for current sale, inventory held for future sale, EOU and inventory held for repair. DLA uses the inventory condition codes as the basis to classify inventory between each category. Controls were not in place to assign inventory the appropriate condition codes. In addition, DLA was unable to determine whether inventory classified as EOU meets the definition in SFFAS No. 3. As a result, DLA was unable to substantiate the amounts classified, presented or disclosed.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Lack of or Inadequate Documentation of Inventory Accounting Policies, Procedures and Controls.** Document, update and finalize the process cycle memoranda (PCM) that document the end-to-end processes for inventory, including receiving, distributing, recording, processing and reporting. Perform a risk analysis and document risks associated with the DLA inventory business process. Review current control documentation and perform a gap analysis for internal controls at the financial statement assertion level.

B. **Lack of or Inadequate Documentation to Substantiate Inventory and Inventory-Related Transactions.**
   - Develop and maintain documentation to support that inventory balances exist and that inventory transactions occurred and are accurately recorded in the financial statements, including:
     - Standardizing data elements included in data extracts from APSRs and the general ledger. For example, data elements to tie material movements to the related financial postings.
     - Standardizing documentation requirements to support financial events.

C. **Lack of or Inadequate Policies, Procedures and Controls Over Inventory Processes.**
   - **Inadequately Designed Controls Over Inventory Processes.** Design and implement internal control activities and include criteria, analyses, reviews and supporting thresholds used in the execution of all relevant internal controls. The control activities should align to and be executed consistently with DLA policies and maintain sufficient documentation to evidence these control activities.
   - **Inventory Held for Others.** Develop policies and procedures related to inventory held for others to include the following:

  - o Properly identifying the inventory owner of the material, as appropriate, such as identifying the owner on material labels upon receipt or segregating the inventory by owner.
  - o Accounting for inventory variances for segregated inventory items with multiple owners so that inventory gains/losses for inventory held on behalf of others are assigned to the appropriate owner.
- **In-Transit and Pipeline Inventory.** Develop and implement policies and procedures to properly validate and reconcile in-transit and pipeline inventory and to validate that balances are complete and accurate.
- **Energy Inventory.** Design policies, procedures and controls to monitor field-level site compliance with DLA Energy policies. The controls should monitor the performance of monthly or quarterly verifications. In addition, DLA should monitor the performance of manual readings on tanks with malfunctioning ATGs.
- **Posting Inventory Adjustments in the General Ledger.** Design application-level controls that prevent users from posting transactions above their approved thresholds. Further, DLA's inventory process should include procedures to review transactions posted to verify that unauthorized transactions were not posted.
- **Inventory Recorded in the Appropriate Period.** Design policies, procedures and controls to process and post transactions to the correct period in the general ledger and to record an accrual at period-end for transactions that should be posted but have not been resolved to reflect recording in the proper period.

D. **Inadequate Policies, Procedures and Related Controls Over Inventory Physical Counts.** DLA should design and implement policies, procedures and controls over inventory physical counts. The inventory count for Supply and Disposition should include a requirement whereby quantities in the perpetual inventory system are supported via physical counts at least once a year, either through a wall-to-wall, year-end count or adequately designed cycle counts in compliance with the DoD FMR.

E. **Lack of Controls for the Reconciliation Between Inventory APSR and the General Ledger.** Design policies and procedures to perform the IRF completely, accurately and timely. The policies should consider the following:
- Reconciling or resolving variances timely, including establishing thresholds for variances that require a review to be performed.
- Including all inventory general ledger accounting codes in the IRF.

F. **Lack of Controls Over Inventory Held by Third Parties.** Design controls over inventory held by third parties by performing a reconciliation of third-party managed inventory balances to the general ledger balances and developing a comprehensive listing of vendors and military services that hold DLA-owned inventory on behalf of DLA. The control activities should include assessing the existence and completeness of inventory held at third parties.

G. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** Design policies and procedures to implement the appropriate accounting standards, specifically SFFAS No. 3 and SFFAS No. 48. The policies and procedures should include:

- Substantiating that the inputs to the MAP calculation include or exclude costs as appropriate.
- Establishing opening inventory balances by valuing inventory using the deemed cost valuation methodologies in accordance with SFFAS No. 48 and verifying that inventory valuation complies with SFFAS No. 3 subsequent to the implementation of SFFAS No. 48.
- Assigning a proper value and unit of measure at the time of receipt.
- Tracking and recording all costs incurred during the kitting or assembly process to the WIP inventory.
- Documenting the methodology, rationale and processes used to estimate valuation allowances for items, including EOU inventory, inventory held for repair, inventory held at net realizable value, etc.

H. **Inadequate or Lack of Controls Over Financial Reporting of Inventory.** Design and implement controls to assign inventory items to the appropriate condition code, including controls over EOU inventory classification in accordance with SFFAS No. 3.

## II. Fund Balance with Treasury

Fund Balance with Treasury (FBwT) represents the aggregate amount of funds in DLA's account with U.S. Treasury. Treasury's Financial Manual (TFM) Chapter 5100, Section 5125 requires agencies to implement effective and efficient reconciliation processes and perform timely reconciliations. However, deficiencies existed in DLA's processes of recording and reconciling transactions involving FBwT.

A. **Lack of or Inadequate Documentation of FBwT Accounting Policies, Procedures and Controls.** DLA did not document the end-to-end process to account for, monitor and report FBwT and FBwT-related transactions.

- **Suspense Accounts.** The documentation did not include the process to correctly identify and resolve suspense amounts.
- **Reconciling Items to Treasury.** The documentation did not include the processes to correct and review Defense Automatic Addressing System (DAAS) rejects; research and resolve differences between U.S. Treasury, disbursing system records, and accounting system records within a timely basis.
- **Monitoring Cash Adequacy.** The documentation did not include processes to review cash balances throughout the year to prepare cash projections and determine whether DLA has enough cash to meet financial obligations.

B. **Inappropriate Policies and Procedures for Recording Cash Collections.** DLA did not have an appropriate process to record FBwT (cash collections) upon receipt. Interfund transactions are not processed by U.S. Treasury until month-end reporting; however, DLA records the cash collection transaction in the general ledger prior to when the transactions occur, resulting in a misstatement of FBwT.

C. **Lack of Controls for the Reconciliation of FBwT Between the General Ledger and the U.S. Treasury.** DLA, in conjunction with DFAS, has implemented the CMR and DRRT processes as mechanisms to attempt to tie the general ledger to U.S. Treasury. However, the CMR and DRRT processes were not sufficient to produce a complete and accurate reconciliation of DLA's general ledger to U.S. Treasury. As a result, DLA was unable to accurately reconcile to U.S. Treasury.

D. **Lack of or Inadequate Documentation to Substantiate FBwT.** DLA was unable to provide listings of collection and disbursement transactions at the detailed voucher level that reconcile to the general ledger. As such, the FBwT transactions are not appropriately supported.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Lack of or Inadequate Documentation of FBwT Accounting Policies, Procedures and Controls.** Finalize the documentation of the end-to-end process for FBwT. The documentation should include the process to perform regular and recurring reconciliations of the suspense account data; the process to identify and correct DAAS rejects timely; the process to research and resolve differences between U.S. Treasury, disbursing system records and accounting system records on a timely basis; and the process to determine that DLA has sufficient cash on hand to meet current financial obligations.

B. **Inappropriate Policies and Procedures for Recording Cash Collections.** Design and implement policies and procedures to properly record a debit to FBwT and a credit to accounts receivable (AR) when the cash transaction has occurred, and cash has been received at U.S. Treasury.

C. **Lack of Controls for the Reconciliation of FBwT Between the General Ledger and the U.S. Treasury.** In coordination with DFAS, obtain a system and organization controls (SOC) report for the processes and controls relevant to DLA, including the CMR and DRRT, and reconcile the transactions recorded in the general ledger to the transactions reported by U.S. Treasury Systems in order to verify that the data was processed correctly.

D. **Lack of or Inadequate Documentation to Substantiate FBwT.** Develop and implement procedures to generate complete and accurate listings of FBwT collections and disbursement transactions at the detailed voucher level that reconcile to the general ledger.

### III. Accounts Receivable and Revenue

Accounts receivable (AR) consists of amounts owed to DLA. Revenue is earned when DLA sells goods and services to the public or other federal entities. AR and revenue fall within the scope of DLA's order to cash process. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls that provide reasonable assurance that revenues applicable to the agency's operations are properly recorded and accounted for to permit the preparation of reliable financial reports and maintain accountability of assets. Because of the nature of DLA's services, DLA has a significant volume of transactions in the order to cash process. This balance represents a substantial portion of their activity that involves receipt of funds by DLA in order to provide inventory to their ultimate consumers. The volume of these transactions makes it critical for DLA to properly record and reconcile these transactions to ensure timely, appropriate recognition of costs to the end users. However, DLA was unable to support the existence of accounts receivable and unfilled customer orders and the occurrence of revenue transactions.

A. **Lack of or Inadequate Documentation of AR and Revenue Accounting Policies, Procedures and Controls.** DLA did not document the end-to-end process to account for Unfilled Customer Orders (UCO), revenue and AR transactions.
   - **UCOs.** The documentation did not include the process to identify, research and resolve unreconciled amounts for UCOs and the process to review the validity of significantly aged UCOs in the general ledger. Additionally, documentation did not include the processes to account for and report UCOs with public customers.
   - **AR.** The documentation did not include the process to evaluate the collectability and validity of significantly aged AR (receivables include a significant amount of aged receivables (greater than 180 days)); the process to review, reconcile or clear negative accounts receivable balances in a periodic and consistent manner; and the process to account for, calculate and post the allowance for doubtful accounts.
   - **Nonstandard Revenue.** The documentation did not include the process for the proper accounting treatment for cash advances received and sales transactions related to nonstandard revenue, such as emergency management situations and disaster relief efforts.
   - **Non-Monetary Exchange Transactions**. The documentation did not include the process for the accounting treatment for non-monetary exchange transactions.
   - **Offsetting Transactions.** The documentation did not include the process and controls to analyze AR and AP transactions to determine proper offsetting, recording and presentation in accordance with the customer or vendor agreement. Additionally, the documentation did not include processes to account for the related budgetary accounts.

B. **Lack of or Inadequate Controls Over AR, Revenue and Cash Collection Processes.** DLA lacked or did not have adequate controls, including the design of controls, over the following:
   - **AR and Cash Collections.** DLA lacked controls to substantiate the validity of AR balances, including the use of a single account for multiple customers and to apply collections from customers accurately and timely. As a result, invalid AR transactions were recorded in the financial statements.

- **Intragovernmental Transactions.** Intragovernmental transactions, including Military Interdepartmental Purchase Requests (MIPRs), are sales orders received from other federal agencies. DLA lacked controls to prevent services from being performed beyond the terms of the agreement and to prevent duplicate transactions from being recorded in the general ledger. As a result, duplicate sales orders were recorded in the general ledger. In addition, there were instances where revenue recorded, in aggregate, exceeded the total funding amount, or the services were performed outside the period of performance.
- **Revenue Recorded Accurately and in the Appropriate Period.** DLA lacked controls to review pricing updates and record revenue transactions appropriately and accurately in the period that the transaction occurred. As a result, a significant number of transactions were not posted using the correct price or were not recorded in the proper accounting period. In addition, the controls to validate that the accruals are recorded at the appropriate amount and in the correct period were not designed effectively.
- **Fuel Exchange Agreements.** DLA did not have adequately designed controls around the fuel exchange agreement (FEA) process. For example, DLA did not reconcile the amounts receivable from, or payable to, foreign governments. In addition, sufficient documentation did not exist to evidence the performance of the control activities. As such, DLA was unable to demonstrate that the control was operating effectively.

C. **Lack of or Inadequate Documentation to Substantiate AR and Revenue Transactions.** DLA was unable to provide documentation that AR and UCO balances exist, or that revenue transactions occurred and are accurately recorded in the financial statements. Specifically, documentation was not available to support that:

- The AR balances (federal and with the public), UCO and deferred revenue transactions are complete and accurate, and reconcile to the general ledger and that the balances exist.
- The revenue transactions recorded, including emergency management situations and disaster relief efforts, are complete and accurate and have occurred. As a result, two of three samples tested were not appropriately supported.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** DLA did not have policies, procedures and controls to effectively implement accounting standards. Specifically, DLA neither implemented nor applied the accounting set forth by SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. DLA performs services for other federal agencies without funding and records receivables from these transactions. DLA was unable to support revenue recognized from unfunded agreements, nor was an analysis performed on the collectability of the receivable related to those agreements. Uncollected billings related to unfunded agreements have been outstanding since FY 2017.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Lack of or Inadequate Documentation of AR and Revenue Accounting Policies, Procedures and Controls.** Document, update and finalize the PCMs that document the end-to-end processes for AR and revenue.
   - **UCOs.** The documentation should include the process to reconcile UCOs between the general ledger and sales legacy module completely, accurately and timely, to review the aged UCO balances for validity and to account for UCOs with public customers.
   - **AR.** The documentation should include the process to evaluate the collectability and validity of significantly aged AR (AR includes a significant amount of aged receivables (greater than 180 days)); the process to review, reconcile or clear negative AR balances in a periodic and consistent manner; and the process to account for calculating and posting the allowance for doubtful accounts.
   - **Nonstandard Revenue.** The documentation should include the financial reporting requirements during emergency management situations, including disaster relief efforts. The policies should include acceptable deviations from the normal business process, documentation requirements and timelines for completion.
   - **Non-Monetary Exchange Transactions.** The documentation should include the accounting and financial reporting requirements for non-monetary exchange transactions.
   - **Offsetting Transactions.** The documentation should include the process and controls implemented to analyze customer and vendor agreements to determine proper offsetting, recording, and presentation of AR and AP transactions and the accounting for the related budgetary accounts.

B. **Lack of or Inadequate Controls Over AR, Revenue and Cash Collection Processes.**
   - **AR and Cash Collections.** Design and implement controls to assess the existence and completeness of the receivable balances, including significantly aged receivables; controls to limit transactions in a customer account to a single customer, rather than a group of customers; and controls to properly, accurately and timely post payments and credits to customer accounts.
   - **Intragovernmental Transactions.** Design and implement controls for intragovernmental transactions that include system controls to prevent services from being provided beyond the terms of the agreement (e.g., period of performance, funding amount) and to prevent duplicate transactions from being recorded in the general ledger.
   - **Revenue Recorded Accurately and in the Appropriate Period.** Design and implement controls to properly record revenue transactions in the appropriate period; controls to review and validate pricing updates; controls to monitor sales transactions at or near period-end; controls to record revenue based on the proper triggering event; controls to manage and maintain documentation to substantiate the revenue transaction; and controls to validate that the accruals are recorded at the appropriate amount and in the correct period.
   - **Fuel Exchange Agreements.** Design, document and implement controls around the FEA process and include criteria, analyses, reviews and supporting thresholds used in the execution of all relevant internal controls.

C. **Lack of or Inadequate Documentation to Substantiate AR and Revenue Transactions.**
- Develop documentation, including detailed listings of account balances, to substantiate that the population of AR (federal and with the public), UCO and deferred revenue transactions are complete and accurate and that the balances in the population exist. The listing should be reconciled to the general ledger.
- Develop documentation to substantiate that the population of revenue transactions recorded, including emergency management situations and disaster relief efforts, are complete and accurate and have occurred.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** Design and implement policies, procedures and controls to properly recognize revenue earned and to assess the collectability of the receivable related to unfunded work orders in accordance with SFFAS No. 7 and the DoD FMR.

**IV. Accounts Payable and Expense**

Accounts payable (AP) consists of amounts owed to vendors. Expenses are incurred and recognized when DLA obtains goods and services from the public or other federal entities. Undelivered Orders (UDOs) represent the amount of goods and/or services ordered which have not been received. AP, expenses and UDOs fall within the scope of DLA's procure to pay process. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls that provide reasonable assurance that expenses and budgetary transactions applicable to the agency's operations are properly recorded and accounted for to permit the preparation of reliable financial reports. Because of the nature of the services, DLA has a significant volume of transactions to procure goods and services to sell to its customers. Deficiencies existed in DLA's processes for recording and supporting AP, expenses and the related budgetary balances; recording transactions in the proper period; documenting policies, procedures and controls; and designing and executing controls over the processes to create and approve obligations and to review, record and pay invoices.

A. **Lack of or Inadequate Documentation of UDO, Unliquidated Obligation (ULO), AP and Expenses Accounting Policies, Procedures and Controls.** DLA did not document the end-to-end processes to account for UDO, AP and expense transactions.
- **UDO.** The documentation did not include the process to review the validity of significantly aged UDO. As a result, there was a significant number of UDO transactions that had no current-year activity.
- **AP.** The documentation did not include the process to evaluate the validity of AP, including significantly aged AP and negative payables; the process to record invoices, including interfund transactions received, in the general ledger and submitted to DFAS for timely payment; and the process to pay invoices timely or assess interest penalties for late payments in accordance with the Prompt Payment Act.
- **Non-monetary Exchange Transactions**. Documentation did not include the process for the proper accounting treatment for non-monetary exchange transactions.
- **ULO.** The documentation did not include the process to review the validity of significantly aged ULO.

- **Offsetting Transactions.** Documentation did not include the process and controls to analyze AR and AP transactions to determine proper offsetting, recording and presentation in accordance with the customer or vendor agreement.
- **Foreign Currency Transactions.** Documentation did not include the process and controls to account for transactions made in foreign currency, including the respective gains and losses.

B. **Lack of or Inadequate Controls Over UDO, ULO, AP, Expenses and Cash Disbursement Processes.** DLA lacked or did not have adequate controls, including the design of controls, over the following:
- **Inadequately Designed Controls Over AP and Expense Processes.** Controls that have been implemented were not designed effectively. For example, the information used in the control activity was not assessed for completeness and accuracy. In addition, sufficient documentation did not exist to evidence the performance of the control activities.
- **UDO.** DLA lacked controls to approve and record obligations in a timely manner; controls to record downward and upward adjustments to UDO accurately and timely; and controls to close invalid UDO in a timely manner. As a result, six of our 11 samples tested were not appropriately supported.
- **Vendor Contracts.** DLA lacked controls to execute contracts in accordance with the Federal Acquisition Regulation (FAR) and record obligations timely for contracts, including Indefinite Quantity Contracts (IQC). For example, IQCs awarded did not have an obligation recorded at the contract award date because the IQC did not have a guaranteed minimum at contract award date.
- **AP and Cash Disbursements.** DLA lacked controls to post goods receipts in a timely manner; review invoices prior to payment; and post payments, including payments that fail to post systematically, in a timely manner.
- **AP and Expenses Recorded in the Appropriate Period.** DLA lacked controls to record AP and expense transactions appropriately and accurately in the period that the transaction occurred.
- **Transactions Recorded at the Detailed Level.** DLA lacked controls to comply with the Federal Financial Management Improvement Act (FFMIA), which requires transactions to be recorded at the detailed level. DLA recorded transactions at a summary level for certain budgetary and proprietary accounts. As a result, each summary-level record contained multiple individual transactions. A reconciliation was not performed between detailed transactions posted to the proprietary accounts and the summarized postings to the corresponding budgetary accounts. Additionally, DLA lacked controls to properly classify vendors as federal or with the public at the transaction level.

C. **Lack of or Inadequate Documentation to Substantiate AP and Expense Transactions.** DLA was unable to provide documentation to support the existence of AP balances, or that expense transactions that occurred were accurately recorded in the financial statements. Specifically, documentation was not available to support the transactions and balances for various accounts, including AP, negative payables, UDO (paid and unpaid) and upward and downward adjustments to delivered and undelivered orders.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** DLA did not have policies, procedures and controls to effectively implement accounting standards. Specifically, DLA neither implemented nor applied the accounting set forth by SFFAS No. 1, *Accounting for Selected Assets and Liabilities,* No. 4, *Managerial Cost Accounting Standards and Concepts;* SFFAS No. 4, *Managerial Cost Accounting Standards and Concepts*; SFFAS No. 5, *Accounting for Liabilities of the Federal Government;* and SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. For example:

- AP and accrued liabilities were not recorded appropriately. For example, DLA policy allows for a liability to be recorded without confirming whether a transfer of title has occurred or service has been rendered. Further, DLA did not have a policy to accrue for contractor services rendered but not submitted within the invoicing system by the end of the month.
- DLA did not match revenue with the related cost of sales where the customers place the order directly with the vendor, such as medical, clothing and textile sales. DLA did not record the revenue earned at the same time the liability was recorded.
- DLA processes allowed for payment without receipt, thus resulting in a negative payable balance. This occurs when payment is made prior to the goods receipts being posted in the general ledger. This resulted in an understatement of expenses and payables, and a misstatement of UDO.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation of UDO, ULO, AP and Expenses Accounting Policies, Procedures and Controls.** Update and finalize the PCMs that document the end-to-end processes for UDO, AP and expenses.

- **UDO.** The documentation should include the process to review the validity of significantly aged UDO, including a process to write off residual UDO for completed transactions.
- **AP.** The documentation should include the process to evaluate the validity of AP, including significantly aged AP and negative payables; the process to record invoices, including interfund transactions received, in the general ledger and submitted to DFAS for payment timely; and the process to pay invoices timely or assess interest penalties for late payments in accordance with the Prompt Payment Act.
- **Non-Monetary Exchange Transactions.** The documentation should include the accounting and financial reporting requirements for non-monetary exchange transactions.

- **ULO.** The documentation should include the process to review the validity of significantly aged ULO, including the process to write off residual ULO for completed transactions.
- **Offsetting Transactions.** The documentation should include the process and controls implemented to analyze customer and vendor agreements to determine proper offsetting, recording, and presentation of AR and AP transactions.
- **Foreign Currency Transactions.** The documentation should include the process and controls to identify, monitor and account for foreign currency transactions.

B. **Lack of or Inadequate Controls Over UDO, ULO, AP, Expenses and Cash Disbursement Processes.**

- **Inadequately Designed Controls Over AP and Expense Processes.** Design and implement internal control activities and include criteria, analyses, reviews and supporting thresholds used in the execution of all relevant internal controls. In addition, evidential matter should be available to demonstrate that the control activity was performed; the scope of the review should be sufficient to identify and correct errors in the procedures performed; and the assessment of any variances should be performed appropriately.
- **UDO.** Design and implement controls to approve and record obligations in a timely manner; controls to record upward and downward adjustments to UDO accurately and timely; and controls to close invalid UDO in a timely manner.
- **Vendor Contracts.** Design and implement controls to execute contracts in accordance with the FAR and record obligations timely for contracts, including IQC. For example, controls that prevent contracts from being completed and executed without the appropriate terms and conditions required by the FAR.
- **AP and Cash Disbursements.** Design and implement controls to post goods receipts in a timely manner; review invoices prior to payment; and post payments, including payments that fail to post systematically, in a timely manner.
- **AP and Expenses Recorded in the Appropriate Period.** Design and implement controls to record AP and expense transactions appropriately and accurately in the period that the transaction occurred and controls to monitor expense transactions at or near period-end.
- **Transactions Recorded at the Detailed Level.** Design and implement controls to comply with the FFMIA and reconcile the transaction-level detail to the summarized postings in each account.

C. **Lack of or Inadequate Documentation to Substantiate AP and Expense Transactions.** Design and implement policies and procedures to retain documentation to support that AP balances exist, or that expense transactions occurred and are accurately recorded in the financial statements.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** Design and implement policies, procedures and controls to record expenses incurred in the proper period; and to match revenue with the related cost of sales in accordance with SFFAS No.1, No. 4, No. 5 and No. 7.

## V. Financial Reporting

Financial reporting encompasses all aspects of operations affecting DLA's ability to produce reliable financial statements and disclosures. This process starts with establishing an effective governance structure to identify and assess risk and continues with developing a control environment that is effective and efficient to manage identified risks. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls to achieve reliable financial reporting. However, deficiencies existed in DLA's processes related to the accumulation and presentation of their financial position and results of operations.

A. **Lack of or Inadequate Documentation of Financial Reporting and Budgetary Policies, Procedures, and Controls.** DLA did not document the end-to-end processes related to financial reporting and funds management.
   - **Financial Reporting.** The documentation did not include the processes to review and reconcile system generated reversals of prior year JVs and processes to review the completeness and accuracy of reports and data used in the financial reporting analyses and controls.
   - **Funds Management.** The documentation did not sufficiently include a description of the process to record budget authority, the transfer process or the Treasury warrant process.

B. **Lack of Controls Over Compliance with the TFM United States Standard General Ledger (USSGL).** DLA did not have controls to configure the general ledger posting logic to be compliant with the USSGL and apply TFM updates timely, nor did DLA have controls to link business events to the correct posting logic. As a result, transactions were not recorded appropriately. For example, DLA inappropriately used a general ledger account (negative payables) to track payments made without goods received. Additionally, DLA did not implement the TFM update to add USSGL account 425400 – Reimbursements and Other Income Earned – Collected From Non-Federal Sources. In addition, the posting logic for various inventory transactions, such as recoupment from returns, disposal and material transfers, and service revenue transactions did not meet the corresponding TFM business events.

C. **Lack of or Inadequate Controls Over Financial Reporting Processes.** DLA lacked or did not have adequate controls, including the design of controls, over the following:
   - **Beginning Balances for Budgetary Accounts.** DLA did not have controls to verify the accuracy of the beginning balances for budgetary accounts, such as Total Actual Resources Collected and Contract Authority Carried Forward accounts. As a result, DLA was unable to substantiate beginning balances recorded on the financial statements.
   - **Trading Partner Transactions.** DLA did not have controls in place to validate and reconcile trading partner eliminations. Adjustments made to AR, AP, revenue, expenses and undisbursed funds were not appropriately supported. A complete reconciliation was not performed at the agreement level to the trading partner adjustments that were being made. As a result, trading partner adjustments were recorded in Defense Departmental Reporting System (DDRS) as "top-side" adjustments and were identified as "unsupported" by DFAS.

- **Contingent Liabilities.** Controls that were implemented were not adequately designed as they did not include sufficient procedures to verify the data used to assess contingent liabilities were complete and accurate.
- **Interfaces Between Feeder Systems and the General Ledger.** DLA did not have adequate controls to interface and post transactions between feeder systems and the general ledger appropriately. As a result, failed interface transactions were not reviewed and resolved in a timely manner.
- **Financial Statement Close Process.** DLA did not have adequately designed controls around the annual close and reconciliation processes, such as the monthly or quarterly reconciliation between the unadjusted trial balance (UTB) and the adjusted trial balance (ATB) was not performed sufficiently and timely; the information used in the reconciliation of UTB to ATB was not complete and accurate; and the review of the procedures performed during the financial statement close process was not adequate. In addition, DLA did not design processes or controls to implement new accounting standards. As a result, DLA has not implemented accounting standards such as SFFAS No. 53 Budget and Accrual Reconciliation and SFFAS 55 Amending Inter-Entity Cost Provisions.
- **Budgetary to Proprietary Tie Points.** DLA did not have adequately designed controls around the tie-point process. There were reconciliation issues between the budgetary and proprietary tie points. As a result, DFAS records unsupported monthly and quarterly JVs in the general ledger and the DDRS to reconcile DLA's budgetary accounts to the proprietary accounts.
- **Monthly or Quarterly JV Adjustments.** DLA did not have controls to review and approve JV adjustments recorded in the general ledger and DDRS by DLA and DFAS for completeness, accuracy and validity. As a result, a comprehensive listing of adjustments made was not maintained to allow DLA to determine the appropriateness and proper recording of each JV adjustment, including those recorded by their service provider.
- **Financial Statement Review Process.** The level of review of the financial statements and footnote disclosures was insufficient to detect and correct misstatements in the financial statements and related disclosures. As a result, inaccurate balances and disclosures were reported in the financial statements and notes. For example, line items were not appropriately classified between federal and with the public; supporting documentation did not support the balances recorded in the notes; and the financial statements were not prepared in conformity with U.S. GAAP as described in Note 1, Significant Accounting Policies, which did not sufficiently describe changes or noncompliance in U.S. GAAP reporting.
- **Transactions Recorded Using Elevated Privileges.** DLA did not have adequate controls to review and approve transactions recorded with elevated access privileges.
- **Accounting for Direct Appropriations.** DLA did not have adequate controls to account for the receipt and expenditure of direct appropriations in the general ledger accurately and in a timely manner.

D. **Lack of or Inadequate Documentation to Substantiate Budgetary Execution.** DLA was unable to provide detailed listings for budgetary accounts at the purchase order (PO) or sales order (SO) level that reconcile to the general ledger, such as delivered and undelivered orders and unfilled customer orders. As such, the budgetary accounts were not appropriately supported.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Lack of or Inadequate Documentation of Financial Reporting and Budgetary Policies, Procedures, and Controls.**
- **Financial Reporting.** Document the financial reporting process, to accurately reflect all aspects of the end-to-end process, including processes and controls performed in providing oversight of service providers. Additionally, evaluate the current policies and procedures for evaluating information produced by the entity.
- **Funds Management.** Document the funds management process and controls to accurately reflect all aspects of the end-to-end budget to execute process, including processes and controls performed by DLA and service providers.

B. **Lack of Controls Over Compliance with the TFM United States Standard General Ledger (USSGL).** Design and implement controls that configure posting logic in the general ledger to be compliant with the USSGL; apply TFM updates in a timely manner; link business events to the correct posting logic; and post transactions as intended.

C. **Lack of or Inadequate Controls Over Financial Reporting Processes.**
- **Beginning Balances for Budgetary Accounts.** Design and implement control activities to accurately state the beginning balance for carryforward budgetary accounts.
- **Trading Partner Transactions.** Design and implement controls to perform a reconciliation at the agreement level to validate trading partner eliminations, which includes identifying, researching and resolving variances between DLA general ledger data and trading partners.
- **Contingent Liabilities.** Enhance control activities to verify the completeness and accuracy around system generated reports used in the execution of controls to identify, estimate, record and disclose contingent liabilities in the financial statements.
- **Interfaces Between Feeder Systems and the General Ledger.** Design and implement controls to review and resolve interface transactions that fail to post to the general ledger on a timely basis.
- **Financial Statement Close Process.** Develop and implement controls around the annual close and reconciliation process, which includes a complete, accurate and timely reconciliation of the UTB to the ATB and processes and controls to analyze the impact of and implement new accounting standards, as appropriate.

- **Budgetary to Proprietary Tie Points.** Design and implement controls to reconcile budgetary to proprietary tie points and investigate variances.
- **Monthly or Quarterly JV Adjustments.** Design and implement controls to review and approve JV adjustments recorded in the general ledger and DDRS by DLA and DFAS for completeness, accuracy, and validity prior to posting.
- **Financial Statement Review Process.** Design and implement controls to sufficiently review the quarterly and annual financial statements and disclosures; to detect and correct misstatements; and to review that the financial statements and disclosures are complete and prepared in accordance with U.S. GAAP.
- **Transactions Recorded Using Elevated Privileges.** Design and implement controls to review and approve transactions recorded with elevated access privileges to assess for completeness, accuracy and validity. The review and approval should be performed by authorized individuals, such as financial management.
- **Accounting for Direct Appropriations.** Develop and implement policies, procedures and internal controls to properly record direct and expended appropriations in the general ledger in an accurate and timely manner.

D. **Lack of or Inadequate Documentation to Substantiate Budgetary Execution.** Develop and implement procedures to generate complete and accurate listings of budgetary accounts at the PO and SO levels that reconcile to the general ledger.

## VI. Oversight and Monitoring

Oversight and monitoring relate to DLA's lack of establishment and implementation of a sufficient enterprise-wide control environment as required by OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management Internal Control*.

A. **Lack of or Inadequate Documentation Around the OMB A-123 Program**. DLA did document the end-to-end process to oversee and monitor the enterprise-level risks and controls, including their OMB A-123 program. Specifically, DLA had not performed and documented a sufficient risk assessment at the enterprise and business process level to assess and document reporting matters, such as the complexity of programs, accounting estimates, related party transactions and extent of manual processes; a complete and accurate population of its assessable units, business processes and relevant controls that are responsive to and mitigate risks, including fraud risks; and an assessment and plan for timely remediation of audit findings.

B. **Lack of or Inadequate Controls Around System Generated Reports.** DLA lacked or did not have adequate controls to verify the accuracy and completeness of system generated reports required in the execution of controls.

C. **Insufficient Oversight and Monitoring of Third-Party Service Providers.** Service organizations undergo examinations of internal controls over systems and processes supporting their customers. The results of these examinations are documented in System and Organization

Controls 1 (SOC 1) reports and include the independent service auditor's report, the service organization's management assertions and identified Complementary User Entity Controls (CUECs) that users of the service organization (e.g., DLA) should have in place to supplement the service organization's internal controls. DLA did not perform sufficient oversight and monitoring of SOC 1 reports and did not sufficiently design, implement or monitor CUECs over its service providers.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation Around the OMB A-123 Program.** Document the end-to-end process to oversee and monitor the enterprise-level risks and controls, including the OMB A-123 program. Perform and document a sufficient risk assessment at the enterprise and business process level to assess and document reporting matters. Document a complete and accurate population of its assessable units and business processes. Identify and assess the risks in each business process, and design and implement relevant controls that are responsive to and mitigate these risks, including fraud risks. Perform an assessment of audit findings and establish and execute the plan to remediate the audit findings timely.

B. **Lack of or Inadequate Controls Around System Generated Reports.** Design and implement controls to verify the accuracy and completeness around system generated reports used in the execution of controls. For example, the procedures should include footing system generated reports; performing a tie-out of system generated reports to the general ledger; verifying that the parameters used to generate the reports or data are appropriate; judgmentally selecting a sample of transactions or balances in the report; and validating that the transactions are accurate.

C. **Insufficient Oversight and Monitoring of Third-Party Service Providers.** Design and implement controls around the SOC 1 review process and validate CUECs are properly identified, designed and operating effectively.

**VII. Information Systems**

Information systems controls are a critical component of the federal government's operations to manage the integrity, confidentiality and reliability of its programs and activities and assist with reducing the risk of errors, fraud or other illegal acts. Information management security, access controls, segregation of duties, configuration management, and IT operations controls are fundamental to the integrity of financial data and can help manage risks such as unauthorized access, changes to critical data, and prevent compromised data. The nature, size, and complexity of DLA's operations require DLA to administer its programs under a decentralized business model by using numerous geographically dispersed operating locations and complex, extensive information systems.

Control deficiencies in the design and operation of financially significant information systems continue to occur in the information systems environment controls. The deficiencies relate to the following areas:

- Access controls
- Configuration management controls
- Segregation of duties controls
- Security management/governance over implementation of security controls
- IT operations controls

**Access Controls**

Access controls include those related to protecting system boundaries, user identification and authentication, authorization, protecting sensitive system resources, audit and monitoring, and physical security. When properly implemented, access controls can help ensure that critical systems assets are physically safeguarded and that logical access to sensitive computer programs and data is granted to users only when authorized and appropriate. Weaknesses in such controls can compromise the integrity of sensitive data and increase the risk that such data may be inappropriately used and disclosed.

The identified access control weaknesses in aggregate represent a significant risk to the DLA financial statements, Information Technology (IT) environment, and financial applications. Absent or ineffective preventative controls and compensating detective controls expose financial systems and financial data to inappropriate access, unauthorized inputs, and inaccurate entries, resulting in significant risk to the financial statements.

The identified access control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- For a selection of users of financially significant applications, access was not restricted to authorized users with a business need, was not reviewed and documented prior to provisioning, and was not assigned in accordance with the principle of least privilege.
- For a selection of account management controls for financially significant applications, user access and activity were not monitored and tracked for routine access recertification, revalidation of privileged access, and terminated or inactive users.
- For a selection of audit logging controls for financially significant applications, audit logs, security violations, and sensitive user activity were not tracked, monitored, resolved, or configured appropriately within systems.

**Configuration Management Controls**

Configuration management involves the identification and management of security features for all hardware and software components of an information system at a given point and systematically controls changes to that configuration during the system's life cycle. By implementing configuration management controls, DLA can ensure that only authorized applications and software programs are placed into production through establishing and maintaining baseline configurations and monitoring changes to these configurations. Weaknesses in such controls can compromise the integrity of sensitive data and increase the risk that such data may be inappropriately used and disclosed.

The identified configuration management and change control weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls expose financial systems and financial data to unexpected impact from changes, inappropriate or unauthorized changes, and application errors in production.

The identified change control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- For a selection of changes to two financially significant applications, both routine and emergency changes were not reviewed, approved, and tested in a non-production environment prior to release. The impact and functionality of configuration changes were not assessed prior to implementation.
- For four financially significant applications, system configurations, baseline code, and production environments were not monitored and inspected for unauthorized changes.
- For two financially significant applications, users had access privileges enabling them to bypass the configuration management process and make changes directly to production.

**Segregation of Duties Controls**

An effective control environment guards against a particular user having incompatible functions within a system. Segregation of duties controls provide policies, procedures, and an organizational structure to prevent one or more individuals from controlling key aspects of computer-related operations and, thereby, conducting unauthorized actions or gaining unauthorized access to financial management information systems.

The identified segregation of duties and conflicting role weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls around segregation of duties allows users to circumvent processes and automated controls in place, obtain unnecessary or elevated access, and impact the integrity of financial data.

The identified weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- Segregation of duties within the user provisioning process were not completed consistently across financially significant applications. Conflicting roles were not inspected and rationalized prior to provisioning. Management did not periodically monitor segregation of duties conflicts that consider both IT and business process roles and activities.
- Application program management has not completely identified sensitive (financial transactions) roles in order to implement appropriate segregation of duties processes and controls.

### Security Management / Governance Over Implementation of Security Controls

An entity-wide information security management and internal control program is the foundation of a security control structure to address security risks. The security management program should establish a framework and continuous cycle of activity for assessing risk, developing and implementing effective security procedures, and monitoring the effectiveness of these procedures. Without a well-designed program, security controls may be inadequate; responsibilities may be unclear, misunderstood, or improperly implemented; and controls may be inconsistently applied. Such conditions may lead to insufficient protection of sensitive or critical resources and disproportionately high expenditures for controls over low-risk resources.

The identified security management and governance weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls around internal controls and governance compound data integrity risk by not monitoring third parties and not remediating known gaps timely.

The identified security management control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- SOC 1 reports were not monitored and reviewed to assess CUECs, including validation of whether management's internal controls relevant to the CUECs, are designed, implemented, and operating effectively.
- Management internal control procedures did not identify financially significant risks, establish and implement controls, track known risk exposure, and remediate control gaps.

### IT Operations Controls

Effective IT operations controls support the reliability of various aspects of operating the IT environment related to the complete and accurate processing of transactions and the protection of information used in that processing. IT operations involves computer job management tasks related to scheduling and running jobs (programs), monitoring the successful completion of those jobs, and detecting and addressing job failures timely. Relevant jobs may accept, process, and move data from one IT application to another via system interfaces for inclusion in financial reporting. IT administrators may also utilize programs or software that supports maintenance of the IT environment or data, including tasks responsible for backing up financially relevant programs and data.

The identified IT operations weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls around IT operations increases the risk that issues with programs that are not scheduled correctly or don't process to completion, may not be addressed, or may be addressed inappropriately, and hardware or software issues will result in the loss of financially relevant data or the ability to accurately process that data.

The identified IT operations control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- Management internal control procedures did not allow them to identify and address transaction errors timely.
- Contingency planning (CP) processes and controls failed in allowing management to backup system data.

***Recommendations***

Implement controls to address deficiencies in access controls, configuration management, segregation of duties, security management procedures, and IT operations to include:

**Access Controls**

- Restrict access to authorized users in accordance with the least privilege principle. Review and approve all access, including justification of business needs.
- Routinely monitor and revalidate access needs for business users, privileged users, and terminated and inactive users.
- Monitor user activity, identify and audit security violations, and assess privileged and sensitive users and transactions.

**Configuration Management Controls**

- Review, approve, and test changes prior to implementation, to include user testing and functionality assessments.
- Monitor source code, configurations, and production environments for unauthorized changes.
- Segregate conflicting roles between development and production environments.

**Segregation of Duties Controls**

- Identify, periodically review, and document sensitive and conflicting roles, enforce established segregation of duties processes, and assess conflicts during account provisioning and management. Segregate conflicting roles where possible, and if unavoidable, document business rationale and monitor user activity.

**Security Management/Governance Over Implementation of Security Controls**

- Establish a process to evaluate and incorporate service provider reports, findings, and controls into management's security documentation, governance process, and application control environment.
- Document risks and controls in place, identify gaps, and complete corrective actions to strengthen the internal control environment. Improve documentation, test and validate controls, and remediate findings.

### IT Operations Controls

- Establish monitoring processes to detect and address transaction errors timely.
- Design and implement controls to periodically backup and monitor system data to successfully respond to incidents and prevent the permanent loss of data.

## Appendix B – Significant Deficiencies

### I. Property, Plant and Equipment

Property, plant and equipment (PP&E) is comprised of general equipment, internal-use software (IUS) and construction-in-progress (CIP). In accordance with FMFIA, management is responsible for establishing and maintaining effective controls to achieve proper accountability for property and other assets for which the agency is responsible. However, DLA was unable to support the existence, completeness, rights and obligations, or valuation of its PP&E.

A. **Lack of or Inadequate Documentation of PP&E Accounting Policies, Procedures and Controls.** PP&E process documentation, policy memoranda and standard operating procedures failed to document the end-to-end processing of PP&E transactions and related internal control activities. Specifically, a complete inventory of CIP has not been performed. DLA is in the process of establishing or revising its policies and procedures for performing these inventories on an ongoing basis.

B. **Lack of or Inadequate Documentation to Substantiate PP&E and PP&E-Related Transactions.** DLA was unable to provide documentation that PP&E balances exist, that transactions occurred or that DLA has rights to the PP&E recorded in the financial statements. Specifically, documentation was not available to support:
   - The completeness and existence of general equipment assets.
   - The validity of PP&E additions and disposals.

C. **Lack of or Inadequate Policies, Procedures and Controls Over PP&E Processes**. DLA lacked or did not have adequate policies, procedures and controls, including the design of controls, over the following:
   - **Inadequately Designed Controls Over PP&E Processes.** Controls that have been implemented were not designed adequately. For example, the information used in the control activity was not assessed for completeness and accuracy. In addition, sufficient documentation did not exist to evidence the performance of the control activities. As a result, DLA was unable to demonstrate that control activities were operating effectively.
   - **IUS.** DLA policy states that IUS assets are recorded as in-service PP&E upon the completion of the asset. However, IUS activity was not evaluated to determine whether the activity should be capitalized or expensed and to identify when assets are completed and should be placed in service.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** DLA did not have policies, procedures and controls to effectively implement accounting standards, causing an inaccurate presentation of PP&E on the balance sheet and in the related footnote disclosure. Specifically, DLA neither implemented nor applied the accounting and valuation methodologies set forth by SFFAS No. 5, *Accounting for Liabilities of the Government*; SFFAS No. 6, *Accounting for Property, Plant and Equipment*; SFFAS No.

10, *Accounting for Internal Use Software*; and SFFAS No. 50, *Establishing Opening Balances for Property, Plant and Equipment*. For example:

- DLA was unable to support the values assigned to general equipment assets, including substantiating that the application of SFFAS No. 6 and SFFAS No. 50 was consistent and appropriate. To account for a significant number of assets that have not been valued, DLA assigned placeholder values to these assets until the valuation process is completed, resulting in misstatements in the financial statements.
- DLA was unable to support the values assigned to IUS assets in accordance with SFFAS No. 10.
- DLA did not establish a policy to account for its leasing arrangements, nor has DLA assessed whether the leasing arrangements should be accounted for as a capital or an operating lease. As a result, the financial statements did not include disclosures for its policy to account for lease arrangements, any operating lease commitments and future minimum payments due.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Lack of or Inadequate Documentation of PP&E Accounting Policies, Procedures and Controls.** Document, update and finalize the PCMs that document the end-to-end processes and controls for PP&E. Complete the inventory of CIP to verify the existence and completeness of the accounting records.

B. **Lack of or Inadequate Documentation to Substantiate PP&E and PP&E-Related Transactions.**
   - Develop documentation to substantiate that all of DLA's general equipment assets are recorded accurately and completely.
   - Assess the data elements in the APSR to allow DLA to differentiate between assets that have been added to or removed from the capital PP&E population and assets that have changed or to assign a unique identifier to each asset that allows for additions and disposals to be identified.

C. **Lack of or Inadequate Policies, Procedures and Controls Over PP&E Processes**
   - **Inadequately Designed Controls Over PP&E Processes.** Design and implement internal control activities that include criteria, analyses, reviews and supporting thresholds used in the execution of all relevant internal controls.
   - **IUS.** Design and implement policies and procedures that require IUS activity to be reviewed for proper capitalization, recorded in the appropriate period and classified appropriately when assets are completed and placed in service.

D. **Lack of Policies, Procedures, and Controls to Effectively Implement Accounting Standards.** Design policies, procedures and controls to implement the appropriate accounting standards, specifically SFFAS No. 5, SFFAS No. 6, SFFAS No. 10 and SFFAS No. 50. The policies, procedures and controls should include:
   - Substantiating the values, including the alternate values, assigned to general equipment assets and that the application of SFFAS No. 6 and SFFAS No. 50 is consistent and appropriate.
   - Assessing whether the values assigned to IUS assets are in accordance with SFFAS No. 10. In addition, evaluate alternative valuation methodologies available under SFFAS No. 50. SFFAS No. 50 permits the exclusion of IUS and IUS under development from the opening balance as of the opening balance date.
   - Establishing an accounting policy to identify and account for leasing arrangements, including whether the leases should be accounted for and reported as capital or operating leases in accordance with SFFAS No. 5 and SFFAS No. 6. In addition, include the required disclosures for capital and operating leases in the financial statements in accordance with OMB A-136.

**II. Environmental Liabilities**

ELs are comprised of cleanup costs associated with the restoration of sites on real property that DLA manages. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls to achieve reliable financial reporting. However, we identified deficiencies in controls listed below, which, when aggregated, we consider to be a significant deficiency.

A. **Inadequate Controls Over Estimation Processes.** DLA did not have effectively designed management review controls to evaluate the completeness and measurement of the EL and the EL recorded in the financial statements. There was a lack of sufficient evidence of management's review, including management's review of the completeness and accuracy of the information used in the valuation of the EL.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Inadequate Controls Over Estimation Processes.** Design and implement formalized management review controls that adequately document management's review of the EL, including establishing a thresholds for review, documentation of findings and actions taken by management.

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# Report of Independent Auditors on Compliance and Other Matters Based on an Engagement to Audit the Financial Statements Performed in Accordance with *Government Auditing Standards*

The Director of the Defense Logistics Agency and the
Inspector General of the Department of Defense

We were engaged to audit, in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States (*Government Auditing Standards)* and the provisions of Office of Management and Budget (OMB) Bulletin No. 24-01, *Audit Requirements for Federal Financial Statements,* the financial statements of the Working Capital Fund of the Defense Logistics Agency (DLA), which comprise the balance sheet as of September 30, 2023, and the related statements of net cost and changes in net position and combined statement of budgetary resources for the year then ended, and the related notes (collectively referred to as the "financial statements"), and have issued our report thereon dated November 8, 2023. Our report disclaims an opinion on the financial statements because DLA continues to have unresolved accounting issues and material weaknesses in internal controls that cause DLA to be unable to provide sufficient evidential support for complete and accurate financial statements on a timely basis.

**Report on Compliance and Other Matters**

In connection with our engagement to audit the financial statements, we performed tests of DLA's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the financial statements, as well as the requirements referred to in the Federal Financial Management Improvement Act of 1996 (FFMIA). However, providing an opinion on compliance with those provisions was not an objective of our engagement, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and the provisions of OMB Bulletin No. 24-01, as described below. Additionally, if the scope of our work had been sufficient to enable us to express an opinion on the financial statements, other instances of noncompliance or other matters may have been identified and reported herein.

Our Report on Internal Control Over Financial Reporting dated November 8, 2023, includes additional information related to the financial management systems and internal controls that were found not to comply with the requirements, relevant facts pertaining to the noncompliance, and our recommendations to the specific issues presented.

As referenced in the Fiscal Year (FY) 2023 DLA Statement of Assurance, DLA provides no assurance that the internal controls over operations, financial systems, reporting and compliance are operating effectively in compliance with the Federal Managers' Financial Integrity Act (FMFIA), Section 4; FFMIA of 1996, Section 803; and *Management's Responsibility for Enterprise Risk Management and Internal Control* OMB Circular No. A-123 Appendix D.

**FFMIA**

Under FFMIA, we are required to report whether DLA's financial management systems substantially comply with federal financial management system requirements, applicable federal accounting standards, and the United States Standard General Ledger (USSGL) at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements. The results of the tests disclosed instances in which DLA's financial management systems did not substantially comply with federal financial management system requirements, applicable federal accounting standards or the USSGL.

(a) Federal financial management system requirements

EY identified as part of the Financial Information Systems material weakness, contained in the Report on Internal Control Over Financial Reporting, noncompliance with federal financial management system requirements for multiple systems. Weaknesses identified include those associated with user access, configuration management/change controls, segregation of duties, security management and IT operations. These financial system deficiencies prevent DLA from being compliant with federal financial management system requirements and inhibit DLA's ability to prepare complete and accurate financial reporting.

(b) Noncompliance with applicable federal accounting standards

As referenced in Note 1 to the financial statements, DLA self-identified that the design of their financial and nonfinancial systems does not allow DLA to comply with applicable federal accounting standards, including not being able to collect and record financial information as required by U.S. generally accepted accounting principles. EY also identified noncompliance with federal accounting standards during our testing, which was included in our Report on Internal Control Over Financial Reporting.

(c) Noncompliance with USSGL posting logic at the transaction level

EY also identified noncompliance with USSGL posting logic during our testing, which was included in our Report on Internal Control Over Financial Reporting.

**FMFIA**

Federal Managers' Financial Integrity Act (FMFIA) of 1982 requires federal entities to establish internal controls, perform ongoing evaluations of the adequacy of the entity's system of internal control, and prepare related reports. The Government Accountability Office's (GAO's) *Standards for Internal Control in the Federal Government* (commonly referred to as the "GAO Green Book") issued under the authority of FMFIA, establishes five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communication and Monitoring. To determine if an entity's internal control system is effective, the Green Book requires management to assess the design, implementation and operating effectiveness of the five components of the entity's internal control system.

DLA has not implemented a formal internal control program that would allow it to substantially comply with FMFIA and the related GAO Green Book requirements, leading to inadequate control environment, risk assessment and monitoring processes.

DLA was not able to provide evidence that they are in compliance with significant aspects of OMB Circular A-123, which implemented FMFIA. DLA provided a FY 2023 Statement of Assurance, however there was not sufficient evidence that DLA fully completed an organizational risk assessment, identified relevant risks related to the financial statement assertions, documented the internal control standards as it relates to those assertions, performed internal control testing, and reported and tracked control deficiencies at the control level for each process identified. DLA provided evidence demonstrating that DLA has started to implement a testing strategy, however, DLA is unable to provide evidence that the extent of testing and review performed is sufficient to meet the requirements of FMFIA.

***DLA's Response to Findings***

*Government Auditing Standards* require the auditor to perform limited procedures on DLA's response to the findings identified in our engagement to audit and described in the accompanying Management's Response to the Audit Reports dated November 8, 2023. DLA's response was not subjected to the other auditing procedures applied in the engagement to audit the financial statements and, accordingly, we express no opinion on the response.

***Purpose of This Report***

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on the entity's compliance. This report is an integral part of an engagement to perform an audit in accordance with *Government Auditing*

*Standards* in considering the entity's compliance. Accordingly, this communication is not suitable for any other purpose.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2023 on our consideration of DLA's internal control over financial reporting. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and the results of that testing, and not to provide an opinion on the effectiveness of DLA's internal control over financial reporting. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DLA's internal control over financial reporting.

Ernst + Young LLP

November 8, 2023

# Management's Response to Audit Reports

DEFENSE LOGISTICS AGENCY
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MEMORANDUM FOR DEPARTMENT OF DEFENSE OFFICE OF THE INSPECTOR GENERAL

SUBJECT: Fiscal Year 2023 Financial Statement Audit

Thank you for the opportunity to comment on Ernst & Young, LLP's Independent Auditor Reports on the Defense Logistics Agency's (DLA) Fiscal Year (FY) 2023 financial statements. DLA remains fully committed to remediating audit findings, improving the accuracy of our financial data and reporting, and making progress towards unmodified audit opinions.

We continue to review audit findings from prior and current financial statement audits and are focused on remediating material weaknesses identified in Ernst & Young, LLP's Report on Internal Control over Financial Reporting. DLA will prioritize Agency requirements to address the scope limitations and align critical milestones within our Audit Roadmaps.

We appreciate Ernst & Young LLP due diligence during the FY 2023 audit. DLA reaffirms our commitment to achieving our audit goals within the Department in support of the Warfighter Always!

Susan J. Goodyear
Susan J. Goodyear
Director, DLA Finance
Chief Financial Officer

# Introduction to the DLA WCF Principal Financial Statements

The DLA WCF principal financial statements and the accompanying notes (financial statements) included in this report are prepared pursuant to the requirements of the CFO Act of 1990 (Pub. L. 101-576) and expanded by GMRA (Pub. L. 103-356) and other applicable legislation. Other reporting requirements include the OMB Circular A-136, as amended. The responsibility for the integrity of the financial information included in these financial statements rests with the management of DLA WCF. The IPA was engaged to perform the audit of DLA WCF's financial statements and disclaimed an opinion on these financial statements. The Audit Report, and Management's Response to the Audit Report, accompany the unaudited financial statements.

## The DLA WCF financial statements consist of the following:

**The Balance Sheets** present those resources owned or managed by DLA WCF that represent future economic benefits (assets), amounts owed by DLA WCF that will require payments from those resources or future resources (liabilities), and residual amounts retained by DLA WCF comprising the difference (net position) as of September 30, 2023 and 2022.

**The Statements of Net Cost** present the net cost of DLA WCF operations for the years ended September 30, 2023 and 2022. DLA WCF's net cost of operations is the gross cost incurred by DLA WCF activities, less any exchange revenue earned and inter-entity eliminations from DLA WCF activities.

**The Statements of Changes in Net Position** present the change in DLA WCF's net position resulting from the net cost of DLA WCF's operations, budgetary financing sources, and other financing sources for the years ended September 30, 2023 and 2022.

**The Combined Statements of Budgetary Resources** present how and in what amounts budgetary resources were made available to DLA WCF, the status of these resources, and the net outlays of budgetary resources for the years ended September 30, 2023 and 2022.

**The Notes to the Principal Financial Statements** provide detail and clarification for amounts in the principal financial statements.

**FEMA and DLA Share Quest for Speed**

Perry Knight, Defense Logistics Agency Distribution Deputy Commander, center, briefs Carla Gammon, Federal Emergency Management Agency Deputy Associate Administrator for Logistics, and Julia Moline for operations recovery, March 7, 2023. **Photo By:** Diana Dawa

# Balance Sheets

As of September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 |
|---|---|---|
| **ASSETS (Note 2)** | | |
| **Intragovernmental** | | |
| Fund Balance with Treasury (Note 3) | $ 5,102,418 | $ 4,702,942 |
| Accounts Receivable, Net (Note 4) | 1,943,993 | 1,545,284 |
| Other Assets (Note 5) | 123,306 | 123,306 |
| **Total Intragovernmental** | **7,169,717** | **6,371,532** |
| **Other than Intragovernmental** | | |
| Accounts Receivable, Net (Note 4) | 920,910 | 725,889 |
| Inventory and Related Property, Net (Note 6) | 23,985,027 | 23,931,134 |
| General Property, Plant and Equipment, Net (Note 7) | 775,756 | 738,862 |
| Advances and Prepayments | 103,477 | 94,303 |
| **Total Other than Intragovernmental** | 25,785,170 | **25,490,188** |
| **TOTAL ASSETS** | **$ 32,954,887** | **$ 31,861,720** |
| **LIABILITIES (Note 8)** | | |
| **Intragovernmental** | | |
| Accounts Payable | $ 150,330 | $ 210,541 |
| Advances from Others and Deferred Revenue | 155,474 | 1,149,354 |
| Other Liabilities: | | |
| Other Current Liabilities - Benefits Program Contributions Payable (Note 9) | 40,065 | 39,558 |
| Other Liabilities (Note 10) | 5 | 5,247 |
| Total Intragovernmental Other Liabilities | 40,070 | 44,805 |
| **Total Intragovernmental** | **345,874** | **1,404,700** |
| **Other than Intragovernmental** | | |
| Accounts Payable | 3,364,850 | 2,705,924 |
| Environmental and Disposal Liabilities (Note 11) | 335,068 | 1,233,787 |
| Federal Employee Benefits Payable (Note 9) | 222,074 | 148,883 |
| Advances from Others and Deferred Revenue | 3,616 | 2,669 |
| Other Liabilities (Note 10) | 306,196 | 323,204 |
| **Total Other than Intragovernmental** | **4,231,804** | **4,414,467** |
| **TOTAL LIABILITIES** | **$ 4,577,678** | **$ 5,819,167** |
| **Commitments and Contingencies (Note 12)** | | |
| **NET POSITION** | | |
| Unexpended Appropriations - Funds from Other than Dedicated Collections | $ 692,700 | $ 988,353 |
| Cumulative Results of Operations - Funds from Other than Dedicated Collections | 27,684,509 | 25,054,200 |
| **TOTAL NET POSITION** | **28,377,209** | **26,042,553** |
| **TOTAL LIABILITIES AND NET POSITION** | **$ 32,954,887** | **$ 31,861,720** |

*The accompanying notes are an integral part of these statements.*

# Statements of Net Cost

For the Years Ended September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 |
|---|---|---|
| **Energy** | | |
| Gross Cost | $ 12,351,624 | $ 11,899,323 |
| Less: Earned Revenue | (13,690,018) | (12,186,946) |
| **Net Cost** | **(1,338,394)** | **(287,623)** |
| **Supply Chain Management** | | |
| Gross Cost | 33,234,056 | 31,599,622 |
| Less: Earned Revenue | (33,482,807) | (30,608,234) |
| **Net Cost** | **(248,751)** | **991,388** |
| **Document Services** | | |
| Gross Cost | 257,123 | 247,576 |
| Less: Earned Revenue | (262,952) | (218,011) |
| **Net Cost** | **(5,829)** | **29,565** |
| **Total Gross Cost** | 45,842,803 | 43,746,521 |
| **Less: Total Earned Revenue** | **(47,435,777)** | **(43,013,191)** |
| **NET COST OF OPERATIONS** | **$ (1,592,974)** | **$ 733,330** |

*The accompanying notes are an integral part of these statements.*

# Statements of Changes in Net Position

For the Years Ended September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 |
|---|---|---|
| **Unexpended Appropriations** | | |
| Beginning Balances | $ 988,353 | $ 198,884 |
| Appropriations Transferred-in/out | 472,636 | 2,767,658 |
| Appropriations Used | (768,289) | (1,978,189) |
| **Net Change in Unexpended Appropriations** | **(295,653)** | **789,469** |
| **Total Unexpended Appropriations: Ending Balance** | **692,700** | **988,353** |
| **Cumulative Results of Operations** | | |
| Beginning Balances | 25,054,200 | 23,914,488 |
| Appropriations Used | 768,289 | 1,978,189 |
| Non-exchange Revenue | (8,168) | 5,231 |
| Transfers-in/out Without Reimbursement | 43,868 | (273,409) |
| Imputed Financing | 229,987 | 165,400 |
| Other | 3,359 | (2,369) |
| **Net Cost of Operations** | **(1,592,974)** | **733,330** |
| **Net Change in Cumulative Results of Operations** | **2,630,309** | **1,139,712** |
| **Cumulative Results of Operations: Ending Balance** | **27,684,509** | **25,054,200** |
| **TOTAL NET POSITION** | **$ 28,377,209** | **$ 26,042,553** |

*The accompanying notes are an integral part of these statements.*

# Combined Statements of Budgetary Resources

For the Years Ended September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 |
|---|---|---|
| **BUDGETARY RESOURCES** | | |
| Unobligated Balance from Prior Year Budget Authority, Net | $ 1,211,122 | $ 3,506,136 |
| Appropriations | 353,116 | 128,730 |
| Contract Authority | 56,778,925 | 52,393,056 |
| Spending Authority from Offsetting Collections | 321,458 | 269,353 |
| **TOTAL BUDGETARY RESOURCES** | **$ 58,664,621** | **$ 56,297,275** |
| **STATUS OF BUDGETARY RESOURCES** | | |
| New Obligations and Upward Adjustments | $ 58,243,603 | $ 55,216,166 |
| Unobligated Balance, End of Year: | | |
| Apportioned, Unexpired Accounts | 421,018 | 1,081,109 |
| Unexpired Unobligated Balance, End of Year | 421,018 | 1,081,109 |
| Total Unobligated Balance, End of Year | 421,018 | 1,081,109 |
| **TOTAL BUDGETARY RESOURCES** | **$ 58,664,621** | **$ 56,297,275** |
| **OUTLAYS, NET** | | |
| Outlays, Net | $ 73,161 | $ 770,937 |
| **AGENCY OUTLAYS, NET** | $ **73,161** | **$ 770,937** |

*The accompanying notes are an integral part of these statements.*

# Notes to the Principal Financial Statements (Unaudited)

## Note 1: Summary of Significant Accounting Policies (Unaudited)

### A. Reporting Entity

Created in 1961, DLA is a component of the U.S. DoD and reports to the OUSD for Acquisition and Sustainment through the Assistant Secretary of Defense for Sustainment. DLA provides material and services to components of DoD (including the U.S. Army, Navy, Air Force, Marine Corps and Space Force), other Federal agencies, and public entities. DLA accomplishes its mission and goals through the operations of the DLA WCF, DLA GF, and DLA NDSTF. These financial statements and accompanying notes herein only refer to the activities of DLA WCF.

The DLA WCF has three major activity groups (DLA Energy, DLA SCM, and DLA Document Services) and two support programs, included within DLA SCM, as described below, to execute its mission to provide supply, logistics, distribution, and disposition service support. These activities are the primary revenue generators within DLA WCF.


**DLA Energy** (Fort Belvoir, Virginia) - provides petroleum products/lubricants, supply chain services, sustainment, restoration and modernization, transportation, aerospace energy, fuel quality/technical support, installation energy and utility services.

**DLA Supply Chain Management:**

Troop Support (Philadelphia, Pennsylvania) - consists of four commodities:

- **Subsistence** – food support for the military all over the world;
- **C&T** - clothing, textiles and equipment to U.S. service members, other Federal agencies, and partner nations;
- **C&E** - construction materials, heavy equipment, tactical gear, firefighting equipment, minerals and precious metals to wood products, imaging and information equipment; and
- **Medical** - medical and pharmaceutical supplies.

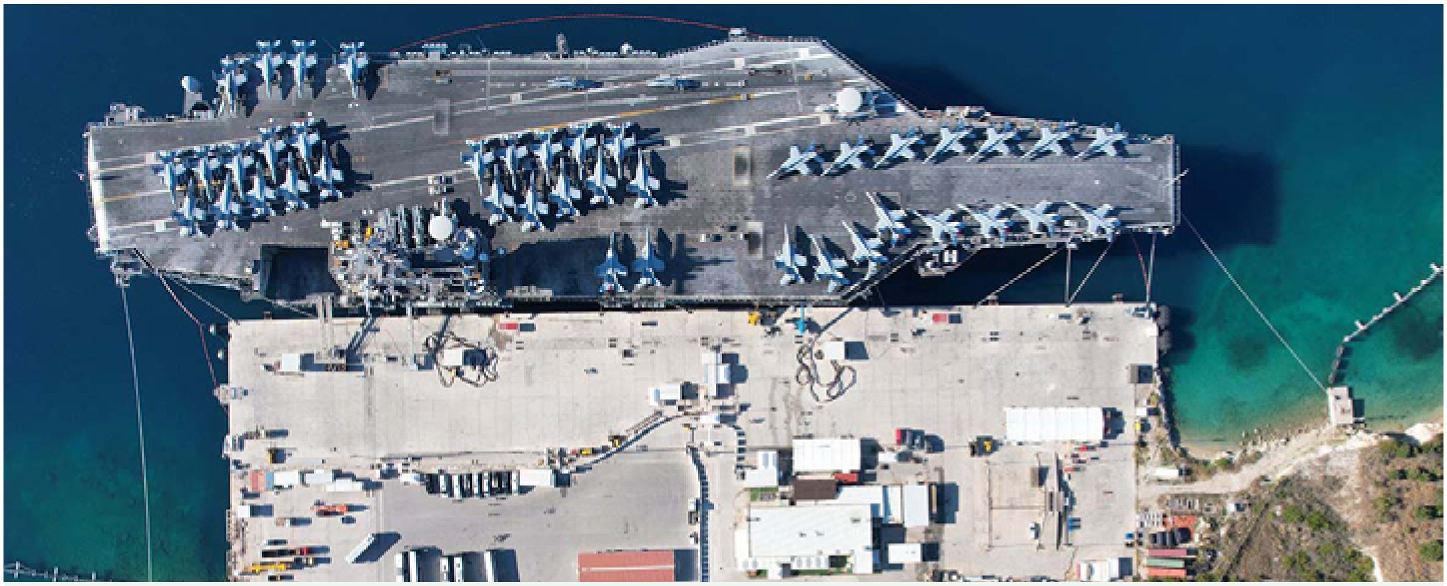
Aviation (Richmond, Virginia) - provides repair parts and industrial items such as screws, nuts, and bolts, typically referred to as bench stock for aviation weapons systems.

Land and Maritime (Columbus, Ohio) - provides repair parts and industrial items such as screws, nuts, and bolts, typically referred to as bench stock for ground-based, maritime, aviation, and foreign military systems.

DLA Support Services Programs - provides distribution support to SCM and may also perform disposition services on behalf of the three DLA Activity Groups, as well as other Federal and public entities.

- **DLA Distribution** (New Cumberland, Pennsylvania) - provides storage and distribution solutions, transportation planning, logistics planning and contingency operations, as well as operating a global network of 34 distribution centers.
- **DLA Disposition Services** (Battle Creek, Michigan) - disposes of excess property by reutilization, transfer, and demilitarization, and conducts environmental disposal and reuse.

**DLA Document Services** (New Cumberland, Pennsylvania) – provides automated document production, printing services, digital conversion, and document storage.



**Souda Bay Scene**

The aircraft carrier USS George H.W. Bush docks at the NATO Marathi Pier Complex in Souda Bay, Greece, Oct. 9, 2022, during a scheduled port visit. **Photo by:** Nikolaos Fragos, Navy

## B. Basis of Presentation and Accounting

**Basis of Presentation and Accounting:** The DLA WCF fiscal year ends September 30. The accompanying financial statements account for all resources for which DLA WCF is responsible. These financial statements present the financial position, results of operations, changes in net position, and the combined budgetary resources of DLA WCF, as required by the CFO Act of 1990, expanded by the GMRA of 1994, and other applicable legislation. The financial statements are prepared from the books and records of DLA WCF activities in accordance with U.S. GAAP, promulgated by the FASAB[4], and presented in the format prescribed by the OMB Circular A-136, except as identified in Note 1.C., *Departures from U.S. GAAP*, and in the following paragraphs.

The DLA WCF financial statements reflect both accrual and budgetary accounting transactions, except as identified in Note 1.C., *Departures from U.S. GAAP*. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when incurred, without regard to the receipt or payment of cash. Budgetary accounting is based on concepts set forth by OMB Circular A-11, which provides instructions on budget execution. Budgetary accounting is designed to recognize the budgetary resources and the related status of those budgetary resources, including the obligation and outlay of funds according to legal requirements, which in many cases is made prior to the occurrence of an accrual-based transaction. Budgetary accounting is essential for compliance with legal constraints and controls over the use of Federal funds.

The DLA WCF is unable to fully prepare financial statements in conformity with and implement all elements of U.S. GAAP (refer to Note 1.C., *Departures from U.S. GAAP*), the form and content requirements for Federal government entities specified by OMB Circular A-136, due to limitations of financial and nonfinancial management processes and systems that support the financial statements. In addition, the financial management systems used by DLA WCF are unable to meet all full accrual and budgetary accounting requirements as many of the financial and nonfinancial feeder systems and processes were not designed to collect and record financial information on the full accrual accounting basis as required by U.S. GAAP. These systems were designed to support reporting requirements for maintaining accountability over assets, reporting the status of Federal appropriations, and recording information on a budgetary basis, rather than preparing financial statements in accordance with U.S. GAAP. Therefore, DLA WCF is continuing the necessary actions required to bring its financial and nonfinancial systems and

[4] FASAB is the official body for setting accounting standards of the U.S. government.

processes to generate financial statements and the accompanying notes in accordance with U.S. GAAP and in compliance with the reporting requirements of OMB Circular A-136. DLA is assessing financial feeder systems and processes and their conformance to existence, completeness, and accuracy requirements as required by U.S. GAAP and OMB Circular A-136. As DLA WCF identifies non-conforming data issues, the Agency will continue to implement interim mitigation processes to address these limitations. In addition, DLA WCF is remediating material weaknesses found in all end-to-end business process cycles pertaining to reconciliations and adequacy of the supporting documentation identified through audits and other compliance reporting.

### Combined Statements of Budgetary Resources:

The budgetary accounting concepts are recognized in the Combined Statements of Budgetary Resources. The Combined Statements of Budgetary Resources present:

(1) budgetary resources for the fiscal year; (2) status of those budgetary resources (includes obligated[5] amounts and unobligated[6] amounts for the fiscal year); and (3) Outlays, Net for the fiscal year, which is comprised of Outlays[7] less Actual Offsetting Receipts (cash transactions). DLA WCF's budgetary resources[8] include unobligated balances of resources from prior years and new resources, consisting of appropriations, contract authority, and spending authority from offsetting collections.

**Intragovernmental and Other than Intragovernmental Transactions:** Statement of Federal Financial Accounting Standards (SFFAS 1), *Accounting for Selected Assets and Liabilities*, distinguishes between Intragovernmental and Other than Intragovernmental assets and liabilities. Intragovernmental assets and liabilities arise from transactions among Federal entities. Intragovernmental assets are claims other Federal entities owe to DLA WCF. Intragovernmental liabilities are claims DLA WCF owes to other Federal entities, whereas Other than Intragovernmental assets and liabilities arise from transactions with public entities. The term "public entities" encompasses domestic and foreign persons and organizations outside the U.S. Government. Other than Intragovernmental assets are claims of DLA WCF against public entities. Other than Intragovernmental liabilities are amounts that DLA WCF owes to public entities. DLA WCF is unable to accurately map its trading partners to separate Intragovernmental and Other than Intragovernmental transactions in accordance with TFM, Volume I, Part 2 Central Accounting and Reporting, Chapter 4700, *Federal Entity Reporting Requirements for the Financial Report of the United States Government.*

The DLA WCF engages in transactions with other DoD and Federal entities that generate inter-DoD and intragovernmental balances; however, DLA WCF is unable to reconcile and resolve differences between balances and transactions with other DoD and Federal entities in accordance with OMB Circular A-136 requirements and TFM, Volume I, Part 2, Chapter 4700, *Federal Entity Reporting Requirements for the Financial Report of the United States Government*. The process is not fully implemented.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions.)

**Intra-departmental Transactions:** DLA WCF is ultimately responsible for the accuracy of its trading partner data and initiating actions to reconcile balances with its trading partners; however, DLA WCF is unable to resolve the reconciling differences in amounts reported for the buyer/ seller transactions reciprocal category with Other Defense Organizations (ODO), (refer to Note 1.C., *Departures from U.S. GAAP*, related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions). A DoD reporting entity unable to provide detail transactions at the appropriate time of the financial statement reporting cycle must adjust its balance to match the seller's or buyer's supportable data.

**Inter-fund Transactions:** Inter-fund transactions and balances among DLA WCF activities (Energy, SCM, and Document Services) are eliminated from the Balance Sheets, the Statements of Net Cost, and the Statements of Changes in Net Position. The Combined Statements of Budgetary

Continued on next page ▶

[5] Per OMB Circular A-11, Section 20, "Obligated amount means a legally binding agreement that will result in outlays, immediately or in the future."

[6] Per OMB Circular A-11, Section 20, "Unobligated amount means the cumulative amount of budget authority that remains available for obligation under law in unexpired accounts.

[7] Per OMB Circular A-11, Section 20, "Outlay means a payment to liquidate an obligation (other than the repayment to the Treasury of debt principal)... Outlays are a measure of Government spending."

[8] Per OMB Circular A-11, Section 20, "Budgetary resources are amounts available to incur obligations in a given year. Budgetary resources consist of new budget authority and unobligated balances of budget authority provided in previous years."

Resources are presented on a combined basis in accordance with OMB Circular A-136; therefore, inter-fund transactions have not been eliminated from these statements. DLA WCF presents the Statements of Net Cost based on activities rather than program costs, which is not in accordance with OMB Circular A-136.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions and Statements of Net Cost).

**Classified Activities:** Accounting standards require all reporting entities to disclose that accounting standards allow certain presentations and disclosures to be modified, if needed, to prevent the disclosure of classified information.

**Use of Estimates:** The DLA WCF management has made certain estimates and assumptions when reporting assets, liabilities, revenue, and expenses and disclosures in the notes. Uncertainties associated with these estimates exist and actual results may differ from these estimates; however, DLA WCF's estimates are based on historical experience, current events and other assumptions that are believed to be reasonable under the circumstances. Significant estimates underlying the accompanying financial statements include: (1) contingent liabilities; (2) E&DL; (3) accruals for accounts receivable related to aerospace, customer direct, Fuel Exchange Agreements (FEA), and inventory accruals; (4) allowance for doubtful accounts; (5) accounts payable MOCAS and outbound MIPR accruals; (6) undelivered orders; (7) Federal Employees' Compensation Act (FECA) liability; (8) inventory defined as Excess, Obsolete, and Unserviceable (EOU); and (9) allowance for inventory held for repair as of the date of these financial statements.

## C. Departures from U.S. GAAP

Financial management systems and processes continue to be evaluated and modified as DLA WCF strives to remediate its material weaknesses and record and report its financial activity in accordance with U.S. GAAP. Therefore, DLA WCF is determining the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with U.S. GAAP. However, due to the financial management systems and operational limitations, the known departures from U.S. GAAP described below that impact DLA WCF financial statements have been identified although other departures from U.S. GAAP may exist that have not been identified.

**Definition of Reporting Entity (Note 1.A.):** The DLA WCF has not completed analyzing material applicable business relationships with other organizations to identify consolidation entities, disclosure entities, or related parties in accordance with SFFAS 47, *Reporting Entity* (effective FY 2018). As a result, DLA WCF is unable to determine if there are consolidation entities that are required to be consolidated and disclosed in DLA WCF financial statements or disclosure entities and related parties where the nature and magnitude of such relationships are required to be disclosed in a Disclosure Entities and Related Parties note to the financial statements.

**Statements of Net Cost:** The DLA WCF does not have policies and compliant processes in place to present its major program costs aligned with DLA WCF mission and goals by responsibility segments in accordance with SFFAS 4, *Managerial Cost Accounting Concepts and Standards*, and OMB Circular A-136.

**Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions (Note 1.B.):** The DLA WCF does not have compliant processes in place to properly report and distinguish between intragovernmental, intra-departmental, and Other than Intra-governmental transactions in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*.

**Inter-Entity Cost (Note 1.U.):** The DLA WCF does not have compliant processes in place to recognize all significant inter-entity costs related to inputs of its goods or services provided to entities for a fee or user charge in accordance with SFFAS 55, *Amending Inter-Entity Cost Provisions*, (effective FY 2019). Generally, the fees and user charges should recover the full costs of those goods and services. Thus, the cost of inter-entity goods or services needs to be recognized by the receiving entity in order to determine fees or user charges for goods and services sold.

**Fund Balance with Treasury (Note 1.G. and Note 3):** The DLA WCF is not able to account for FBwT in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, due to its inability to identify and reconcile the reported differences between DLA WCF's accounting system and Treasury. Monthly unsupported journal vouchers are made to adjust the FBwT balances in DLA WCF financial statements to match U.S. Treasury records.

**Accounts Receivable, Net, Revenue, and Unfilled Customer Orders (Notes 1.H. 1.U. and 1.W., Notes 4; Note 6; and Note 13):** The DLA WCF does not have policies and compliant processes in place to: (1) recognize revenue and record the related accounts receivable, net and unfilled customer order (UCO) balances from goods sold and services provided in the proper period; (2) identify, evaluate, record, and report an allowance for doubtful accounts related to intragovernmental receivables in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, and Technical Bulletin 2020-1, *Loss Allowance for Intragovernmental Receivables*; and (3) adjust revenue to the extent that realization of the full amount is not probable in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, and SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. More specifically:

Direct Sales - DLA WCF Holds the Inventory to be Sold: In some instances, the current distribution system that DLA WCF uses is not in accordance with SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, as revenue may be recognized before materials are shipped or delivered to the customer;

Consignment/Direct Sales - Third Party Holds the Inventory to be Sold: For inventory that is managed by a third party, revenue is recognized on the date DLA WCF bills the customer which may occur before DLA WCF releases control of the materials, which is not in accordance with SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*;

Customer Direct Sales: The customer direct process is where DLA WCF permits its customers to order goods directly from DLA WCF's authorized vendors. Under DLA WCF's business structure, DLA WCF has the obligation to pay the vendor and the right to collect payment from the customer. Therefore, DLA WCF incurs a liability and earns revenue at the time the customer accepts the goods from the vendor. However, while DLA WCF records an accrual for the liability incurred, DLA WCF does not account for the revenue earned at the same time in accordance with SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*;

Customer Returns: The DLA WCF does not match the customer returns to the original sales orders and improperly decreases revenue, cost of goods sold, and contract authority liquidated for the amount of the return, which is not in accordance with SFFAS 3, *Accounting for Inventory and Related Property*, and SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*;

Fuel Exchange Agreement Business Process: The DLA WCF does not have policies and compliant processes in place to: (1) properly adjust the budgetary accounts in accordance with SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, when the netting of individual sales and purchase transactions occur; (2) recognize and value appropriately the replacement-in-kind transactions in accordance with SFFAS 3, *Accounting for Inventory and Related Property*; and (3) demonstrate that the monthly accrual methodology for FEA is in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*, and SFFAS 1, *Accounting for Selected Assets and Liabilities*;

Unfilled Customer Orders: The DLA WCF does not properly record UCO activity and is unable to support the UCO balance in the accounting system in accordance with SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*;

Revenue: The DLA WCF performs services for other Federal entities and recognizes accounts receivable and revenue for these transactions without assessing the probability of collection which is not in accordance with Technical Bulletin 2020-1, *Loss Allowance for Intragovernmental Receivables* SFFAS 1, *Accounting for Selected Assets and Liabilities*, and SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. In addition, DLA is unable to produce a population of customer disputes which impacts their ability to support the allowance for returns in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities,* and SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*; and

Foreign Currency: The DLA WCF does not have a policy and compliant processes in place to determine the significant effects, if any, of changes in the exchange rate related to recording foreign currency transactions in accordance with SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. This also impacts accounts payable.

**Inventory and Related Property, Net (Note 1.J. and Note 6):** The DLA WCF does not have policies and compliant processes in place to account for inventory and related property, net or properly account for gains and losses on adjustments to inventory in situations where DLA WCF owns the same material as held for a customer or held as EOU in accordance with SFFAS 3, *Accounting for Inventory and Related Property*, and SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. Furthermore, DLA has not completed establishing inventory and related property beginning balances using deemed cost and has not made an unreserved assertion as permitted by SFFAS 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials*, (effective FY 2017). More specifically:

Excess, Obsolete, Unserviceable: The DLA WCF does not have procedures in place to review and determine if additional material in its accounting system should be classified as EOU in accordance with SFFAS 3, *Accounting for Inventory and Related Property*. Upon receipt of EOU from other components or military services, the asset is recorded incorrectly as a gain rather than a transfer-in. Upon disposition of EOU, the expense is recorded incorrectly as cost of goods sold rather than determining the gain or loss based on the difference of the sale price and Net Realizable Value (NRV) in accordance with SFFAS 3, *Accounting for Inventory and Related Property*. The accounting treatment for both transfers-in and disposition of EOU is not in accordance with SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*.

The DLA WCF is unable to determine the carrying value of the inventory before it was identified as EOU inventory, in accordance with SFFAS 3, *Accounting for Inventory and Related Property*;

Raw Materials and Inventory Work in Process: The DLA WCF does not properly account for inventory provided to vendors against contracts and work orders for manufacturing and assembly in accordance with SFFAS 3, *Accounting for Inventory and Related Property*. These items should be initially accounted for as raw material, and then as inventory Work in Process;

Additional Inventory Costs: The DLA WCF does not properly account for additional inventory costs in the manufacturing and assembly process, in accordance with SFFAS 3, *Accounting for Inventory and Related Property*;

Categories of Inventory: The DLA WCF does not have policies and procedures in place for management's criteria to determine the category of inventory in accordance with SFFAS 3, *Accounting for Inventory and Related Property*;

Customer Direct: The DLA WCF does not record Customer Direct transactions in accordance with SFFAS 3, *Accounting for Inventory and Related Property*. DLA WCF combines the purchase from the vendor and the cost of goods sold into a single entry in the accounting system that does not include the receipt or issuance of inventory; and

**Relief Prep**

Soldiers pack a military vehicle full of food, water and tarps for distribution in Englewood, Fla., Oct. 5, 2022, during Hurricane Ian relief efforts. **Photo By:** Army Spc. Christian Wilson

Goods Receipt: The DLA WCF does not have sufficient policies and procedures to properly account for receipts of goods when the received quantity does not match the purchase order quantity in accordance with SFFAS 3, *Accounting for Inventory and Related Property*. In addition, under the contractual agreement, if the contractor delivers and DLA WCF receives quantities of any item in excess of the quantitties called for, DLA WCF may retain such excess quantities without compensating the contractor. Rather than adjusting the unit cost based on the updated quantity received, DLA WCF is recording a gain to account for the excess items.

**General Property, Plant and Equipment, Net (Note 1.K and Note 7):** The DLA WCF does not have policies and compliant processes in place to account for general PP&E, net, at historical cost, in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment*, and SFFAS 10, *Accounting for Internal Use Software*. Supportable general PP&E beginning balances have not been established for buildings, general equipment, CIP, Internal Use Software (IUS), and IUS in Development using the alternative valuation methods permitted by SFFAS 50, *Establishing Opening Balances for General Property, Plant, and Equipment*, (effective FY 2017). In addition, DLA WCF does not have compliant processes in place to account for impairment of facilities and equipment in accordance with SFFAS 44, *Accounting for Impairment of General Property, Plant, and Equipment* Remaining in Use. More specifically:

Transferred assets: The DLA WCF is unable to determine the valuation of general equipment assets previously transferred from the military services in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment*;

Internal-Use Software: The DLA WCF is unable to substantiate the valuation of internal-use software in accordance with SFFAS 10, *Accounting for Internal Use Software,* and SFFAS 50, *Establishing Opening Balances for General Property, Plant, and Equipment*;

Internal-Use Software in Development: The DLA WCF does not have the proper policies and compliant processes to identify IUS in Development balances in accordance with SFFAS 10, *Accounting for Internal Use Software*;

Construction-in-Progress Balances: The DLA WCF does not have the proper policies and compliant processes to identify aged CIP balances in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment*;

Capitalization: The DLA WCF does not properly follow the policies and procedures to effectively implement and consistently apply the capitalization threshold, in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment,* and SFFAS 10, *Accounting for Internal Use Software*;

Depreciation: The DLA WCF does not properly follow the policies and procedures to effectively implement and consistently apply depreciation and amortization, in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment,* and SFFAS 10, *Accounting for Internal Use Software*;

Rights and Obligations: The DLA WCF is unable to substantiate whether DLA WCF has the rights and obligations to the recorded general PP&E assets in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment.*

**Leases (Note 1.L.):** The DLA WCF does not have policies and compliant processes in place to identify, evaluate, record, and report capital and operating leases in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*, and SFFAS 6, Accounting for Property, Plant, and Equipment. As such, DLA WCF does not have any capital or operating leases reported or disclosed as of September 30, 2023 and 2022.

**Advances and Prepayments (Note 1.M.):**
The DLA WCF does not have policies and compliant processes in place to record advances and prepayments related to organic manufacturing and outstanding contract financing payments in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*. Specifically, the accounts payable adjustment methodology for negative payables is inaccurate and does not comply with TFM/USSGL posting logic.

**Accounts Payable, Expenses, and Undelivered Orders (Notes 1.O. and 1.W; Note 8; and Note 14):** The DLA WCF does not have policies and compliant processes in place to account for accounts payable, expense accruals, and the related Undelivered Orders (UDOs) in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, and SFFAS 5, *Accounting for Liabilities of the Federal Government*. More specifically:

Continued on next page ▶

**Accrual Methodology for Liabilities:** The DLA WCF does not properly accrue liabilities in the period incurred, recognize the related expenses, and reduce UDOs in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*;

**Capitalized Expenses:** The DLA WCF does not properly recognize in its accounting records the full cost of the goods or services it receives as an expense in accordance with SFFAS 4, *Managerial Cost Accounting Standards and Concepts;*

**Negative Payable:** The DLA WCF processes allow for payment without receipt, thus resulting in a negative payable that is not in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*. This occurs when a payment is made prior to the goods receipts being posted in DLA WCF's accounting system. This results in an understatement of current year expenses and payables, and an overstatement of UDOs; and

**Undelivered Orders:** The DLA WCF does not have sufficient policies and procedures in place to record obligations at the time contracts are awarded in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*. In addition, DLA WCF is unable to support the UDO balance in the accounting system.

**Environmental and Disposal Liabilities (Note 1.P; Note 11; and Note 12):** The DLA WCF does not have policies and compliant processes in place to reconcile asset listings to the amounts recorded for E&DL related to cleanup, asset closure, and asbestos associated with general PP&E, in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*; SFFAS 6, *Accounting for Property, Plant, and Equipment*, and Federal Financial Accounting and Auditing Technical Release 2, *Determining Probable and Reasonably Estimable for Environmental Liabilities in the Federal Government*.

**Commitments and Contingencies (Note 1.N; Note 10; Note 11; and Note 12):** The DLA WCF does not have policies and compliant processes in place to reconcile asset listings to the amounts recorded for E&DL related to cleanup, asset closure, and asbestos associated with general PP&E, in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*; SFFAS 6, *Accounting for Property, Plant, and Equipment*, and Federal Financial Accounting and Auditing Technical Release 2, *Determining Probable and Reasonably Estimable for Environmental Liabilities in the Federal Government*.

**Reconciliation of Net Cost to Net Outlays (Note 15):** The DLA WCF does not have an established policy for the reconciliation of net cost to net outlays in accordance with SFFAS 53, *Budget and Accrual Reconciliation*. DLA WCF is also unable to fully prepare reconciliation of net cost to net outlays in conformity with U.S. GAAP due to limitations of financial and nonfinancial management processes and systems that support the underlying financial information.

**Public-Private Partnerships:** The DLA WCF has not completed analyzing all applicable business relationships to determine if these arrangements or transactions indicate the existence of Public-Private Partnership (P3) relationships, risk-sharing arrangements or transactions lasting more than five years between public and private sector entities, in accordance with SFFAS 49, *Public-Private Partnerships: Disclosure Requirements*, (effective FY 2019). As a result, DLA WCF is unable to determine the nature of such partnerships, if applicable, and related Federal funding amounts required to be disclosed in a P3 note to the financial statements.

**Loading Labor**
Florida National Guardsmen load a pallet of water into an Army Chinook helicopter in Fort Myers, Fla., Oct. 3, 2022, in response to Hurricane Ian. **Photo By:** Air Force Senior Airman Jesse Hanson

## D. Pronouncements Recently Issued but Not Yet Effective

FASAB has issued the following pronouncements that may affect future financial presentation, as well as financial management practices and operations of DLA WCF upon implementation. DLA WCF has not completed the process of evaluating the effects of adopting these pronouncements and is unable to determine the materiality of changes that adopting them will have on its financial position, results of operations, changes in net position, and combined budgetary activity.

| FASAB Statement No | SFFAS 54 | SFFAS 57 (paragraphs 3 – 8, 11, and 12) | SFFAS 60 | SFFAS 61 |
|---|---|---|---|---|
| FASAB Standard | Leases: An Amendment of SFFAS 5, *Accounting for Liabilities of the Federal Government*, and SFFAS 6, *Accounting of Property, Plant, and Equipment* | Omnibus Amendments FY 2019 | Omnibus Amendments FY 2021 | Omnibus Amendments FY 2023 |
| Adoption Required in FY | Deferred to FY 2024 | Effective FY 2024 | Effective FY 2024 | Effective FY 2024 |

SFFAS 54, *Leases: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government,* and SFFAS 6, *Accounting for Property, Plant, and Equipment*, revises the current Federal financial reporting standards for lease accounting and requires that Federal lessees recognize a lease liability and a leased asset at the commencement of the lease term, unless it meets any of the scope exclusions or the definition/criteria of short-term leases, or contracts or agreements that transfer ownership, or intragovernmental leases. SFFAS 57, *Omnibus Amendments 2019*, SFFAS 60, *Omnibus Amendments 2021: Leases-Related Topics,* and SFFAS 61, *Omnibus Amendments 2023: Leases-Related Topics ll*, amend certain references to leases affected by SFFAS 54, as well as other minor changes in order to improve clarity of existing statements.

## E. Appropriations and Funding

**Initial Corpus:** The DLA WCF received its initial corpus through an appropriation from the DWWCF. The corpus financed initial operations to obtain goods and services sold to customers on a reimbursable basis to maintain the corpus. In addition, DLA WCF receives direct or supplemental appropriations through DoD reprogramming actions, Title V (Revolving and Management Funds), IX (Overseas Contingency Operations), and X (Required Additional Appropriations). For the years ended September 30, 2023 and 2022, DLA WCF received direct appropriations in the amount of $472.6 million and $2.8 billion, respectively (refer to Note 14, Statement of Budgetary Resources).

The DWWCF consists of six activity groups. DLA WCF operates three of the six activity groups, which include DLA Energy, DLA SCM, and DLA Document Services. DFAS and the DISA operate the other three activity groups. DLA WCF is the cash manager for the DWWCF funding and is responsible for developing DWWCF activity group budget exhibits related to cash and monitoring cash execution. Although DLA WCF shares its accounting code with DFAS and DISA, each agency receives their own separate Annual Operating Budget. OUSD(C) uses a data element referred to as a 'limit' to differentiate the various ODOs under Treasury Index (TI)-97. DLA WCF uses limits assigned to the TI-97 organizations to track spending at a level below the Treasury Account Symbol (TAS) level.

**Contract Authority:** The DLA Energy and DLA SCM receive contract authority for their operating and capital programs. Contract authority is a type of budget authority that permits obligations to be incurred in advance of an appropriation, offsetting collections, or receipts to make outlays to liquidate the obligations. Typically, the Congress provides contract authority in an authorizing statute to allow DoD components to incur obligations in anticipation of the collection of receipts or offsetting collections that will be used to liquidate the obligations. Subsequently, the contract authority liquidates through the receipt of customer funds.

**Spending Authority from Offsetting Collections:** The DLA Document Services receives spending authority from offsetting collections for its operation program. Spending authority from offsetting collections represent authority that permits obligations and outlays to be financed by reimbursements from the funding agencies and requires the receipt of customer orders prior to incurring obligations.

## F. Entity and Non-Entity Assets

The DLA WCF reports both entity and non-entity assets. Entity assets are assets that the reporting entity has authority to use in its operations. Management may have authority to decide how funds are used or it may be legally obligated to use the funds a certain way. Non-entity assets are not available for use in DLA WCF's operations. DLA WCF maintains stewardship accountability and reporting responsibilities for non-entity assets and will subsequently remit these non-entity assets to the Treasury. DLA WCF records a corresponding liability, custodial liability, for these accounts receivable. (Refer to Note 2, *Non-Entity Assets*, and Note 10, *Other Liabilities*).

## G. Fund Balance with Treasury

The DLA WCF does not maintain cash in a commercial bank, but rather in the U.S. Treasury. DLA WCF's FBwT includes the amount available for DLA WCF to pay current liabilities and finance authorized purchases, except as restricted by law. The disbursing offices of DFAS, the U.S. Army Corps of Engineers, GSA, and the Department of State's financial service centers process DLA WCF's cash collections, disbursements, and adjustments.

In recent years, DLA WCF implemented Treasury Direct Disbursing (TDD), which provides DLA WCF the capability to transmit directly from accounting systems to Treasury for disbursements. With the implementation of TDD, DLA WCF has a unique accounting code allowing DLA WCF to identify the transactions.

On a monthly basis, DLA WCF adjusts its FBwT account balance to bring its cash balance in agreement with the U.S. Treasury cash balance reported on the Central Accounting and Reporting System using the Cash Management Report (CMR). The CMR provides a summary cash position for each ODO's FBwT account by fiscal year and appropriation at the limit level. The adjustments represent the undistributed disbursements and collections amounts that have been reported to Treasury but have not yet been posted to DLA WCF's accounting systems. Undistributed amounts can be a result of timing, invalid line of accounting, invalid TAS information, and unsupported and unreconciled differences.

The DLA WCF's accounting service provider, DFAS, uses suspense accounts to hold transactions temporarily prior to identifying the correct funding. Suspense account items represent the amounts that are reported to U.S. Treasury at the Treasury Index (TI) Level (TI-17, TI-21, TI-57, TI-97), but have not yet been classified to a DLA WCF TAS. The transactions in suspense accounts include unidentified collections, disbursements, recyclable materials, and Intragovernmental payment and collection transactions at month end. DFAS researches suspense transactions to post them against the appropriate line of accounting. The current balances for DLA WCF suspense transactions are derived from the DFAS Suspense Account Universe of Transactions (UoT).

U.S. Treasury also compares DoD's FBwT reported by DFAS with comparable data submitted by financial institutions and U.S. Treasury Regional Financial Centers and notifies DoD of differences in collection and disbursement data on the Statement of Differences (SOD) report. The current balances for DLA WCF SOD transactions are derived from DFAS management analysis and the SOD UoT.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Fund Balance with Treasury, and Note 3, *Fund Balance with Treasury*).

## H. Accounts Receivable, Net

**Accounts Receivable, Net:** Accounts Receivable represent amounts due to DLA WCF from other Federal entities (Intragovernmental) and the public (Other than Intergovernmental). DLA's accounts receivable arise from sales of inventory, services performed and interest receivable.

DLA WCF presents its accounts receivable net of an allowance for doubtful accounts, which is based on a systematic methodology of grouped aged public and Federal accounts receivables. DLA WCF evaluates the allowance methodology and estimated allowance percentages quarterly based on historical average collections on aged public and Federal accounts receivable. The allowance for doubtful accounts is calculated based on the aged accounts receivable balances from the preceding month, with the exception of FEA accounts receivable, as these are reconciled in periodic settlements with the foreign governments (refer to Note 1.W, *Transactions with Foreign Governments and International Organizations*, for additional information on FEA sales and settlements).

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Intragovernmental/Intra-departmental and Other than Intragovernmental transactions and Accounts Receivable, Net, Revenue, and Unfilled Customer Orders, Note 4, *Accounts Receivable, Net*)

## I. Other Assets

The DLA WCF other assets include the Strategic Petroleum Reserve. DLA Energy's Strategic Petroleum Reserve consists of crude oil held by the Department of Energy (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. 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. As of September 30, 2023 and 2022, none of the reserve has been drawn upon, therefore the full inventory remains on hand with DoE (Refer to Note 5, *Other Assets*).

## J. Inventory and Related Property, Net

The DLA WCF inventory is comprised of material held at DLA Energy and DLA SCM and categorized into:

**Inventory Held for Sale:** Inventory that is in the process of production for sale or to be consumed in the production of goods for sale or in the provision of services for a fee (refer to Note 1.A., *Reporting Entity*), for items held for sale by activity group. Additionally, DLA WCF has inventory held for sale, in-transit. This consists of material in-transit from commercial and Government suppliers to the financial reporting entity or material in transit between storage locations.

In FY 2023, DLA GF transferred Inventory Held for Sale to DLA WCF. Upon request, DLA WCF will transfer these assets, without reimbursement, to the Military Departments in accordance with DoD policy.

**Inventory Reserved for Future Sale:** Inventory that is maintained and not readily available in the market or because there is more than a remote chance that they will eventually be needed (although not necessarily in the normal course of operations). Similar to the Inventory Held for Sale, the inventories primarily include weapon system repair parts from DLA Aviation and DLA Land and Maritime, and food and medical supplies from DLA Troop Support.

**Inventory Held for Repair:** Inventory that is damaged and requires repairs to make it suitable for sale, which includes consumable spares, repair parts and repairable items.

**Excess, Obsolete, and Unserviceable Inventory:** Excess inventory exceeds management requirements to meet DLA WCF's mission. Obsolete inventory is no longer needed due to technology, laws, customs, or operations. Unserviceable inventory is damaged inventory that is more economical to dispose of than to repair.

**Inventory Valuation:** The DLA WCF uses the Moving Average Cost (MAC) method to value Inventory Held for Sale, Reserved for Future Sale and Held for Repair, as described in SFFAS 3, *Accounting for Inventory and Related Property*, and DoD Financial Management Regulation (FMR), Volume 4, Chapter 4. Inventory Held for Repair is valued at MAC less an allowance for the estimated repair cost. The allowance is calculated based on 2.0% of the total value of Inventory Held for Repair. The MAC is calculated each time inventory is purchased dividing the total cost of units available by the number of total units available.

EOU inventory is valued at its expected NRV. An NRV factor is applied to the assets' original acquisition value to determine NRV. The FY 2023 NRV calculation resulted in an NRV of zero as of September 30, 2023.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Inventory and Related Property, Net, and Note 6, *Inventory and Related Property, Net.*)

## K. General Property, Plant and Equipment, Net

The DLA WCF general PP&E consists of CIP, IUS, IUS in development, and general equipment that are used to facilitate the Agency's mission. The land that these assets reside on is not owned by DLA WCF.

**Capitalization Threshold:** The DLA WCF general PP&E assets are recorded at historical acquisition cost plus improvements when an asset has a useful life of two or more years, and the acquisition cost exceeds the $250,000 capitalization threshold, effective October 1, 2013. The general PP&E assets acquired prior to October 1, 2013, were capitalized at various thresholds and are carried at the remaining net book value. However, some of the assets capitalized after October 1, 2013 do not exceed the $250,000 capitalization threshold.

In FY 2020, DLA WCF transferred real property assets to the Military Departments and is in process of establishing Memorandum of Agreements (MOAs) with the Military Departments for the use of real property and the recording of related imputed costs, in accordance with DoD policy.

The DLA WCF continues to validate its general PP&E balances by verifying the existence and completeness, confirming rights and obligations by validating documentation from the military services to ensure DLA WCF is the appropriate Financial Reporting Organization (FRO), and documenting processes through reviewing and updating policy guidance to define the procedures used for the valuation method. DLA WCF has not yet finalized the inventory and valuation process for their general PP&E. Accordingly, DLA WCF has not made an unreserved assertion that the opening balances of general PP&E for FY 2023 are presented fairly in accordance with U.S. GAAP and SFFAS 50, *Establishing Opening Balances for General Property, Plant, and Equipment.*

The DLA WCF determines the useful life of its general PP&E using the asset classification and the type of assets based on the DoD FMR 7000.14-R Volume 4, Chapters 24, 25, 27 and the OUSD Memorandum *"Financial Reporting Policy for Real Property Estimated Useful Lives, Land Valuation, and Accounting for Real Property Outside of the United States."*

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to General Property, Plant and Equipment, Net; Note 1.P.*, Environmental and Disposal Liabilities*; and Note 7, *General Property, Plant, and Equipment, Net*)

## Depreciation Method and Useful Life

| Asset Classes | Depreciation/ Amortization Method | Useful Life (Years) |
|---|---|---|
| IUS | Straight-line | 2, 5 or 10 |
| General Equipment | Straight-line | 5 or 10 |
| CIP | Not Applicable | Not Applicable |
| IUS in development | Not Applicable | Not Applicable |

## L. Leases

As of September 30, 2023 and 2022, DLA WCF has not completed the process of developing policies and procedures to identify, evaluate, record, and report capital and operating leases  in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*, and SFFAS 6, *Accounting for Property, Plant, and Equipment,* (refer to Note 1.C., Departures from U.S. GAAP, related to Leases.)

## M. Advances and Prepayments

**Advances:** Assets such as civil service employee pay and travel advances, and certain contract financing payments not reported elsewhere in DLA WCF Balance Sheets.

The DLA SCM 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 WCF may provide financing payments. The Federal Acquisition Regulation, Part 32, defines contract financing payments as "authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government".

**Prepayments:** Payments made in advance of the receipt of goods and services. DLA WCF's policy is to expense and/or properly classify assets when the related goods and services are received.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Advances and Prepayments.)

## N. Commitments and Contingencies

In accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*, as amended by SFFAS 12, *Recognition of Contingent Liabilities Arising from Litigation: An Amend-*

*ment of SFFAS 5, Accounting for Liabilities of the Federal Government,* DLA WCF evaluates all contingent liabilities based on three criteria: probable, reasonably possible and remote. DLA WCF recognizes contingent liabilities in DLA WCF's Balance Sheets and Statements of Net Cost when the loss is determined to be probable and reasonably estimable. DLA WCF discloses those contingencies that are reasonably possible in Note 12, *Commitments and Contingencies.* DLA WCF does not disclose or record contingent liabilities when the loss is considered remote.

The DLA WCF recognizes that the estimated liability may be a specific amount or a range of amounts. If an amount within the range is a better estimate than any other amount within the range, that amount is recorded. If no amount within the range is a better estimate than any other amount, the minimum amount of the range is recorded and the range and a description of the nature of the contingency are disclosed.

In the event of an adverse judgment against the Government, some of the liabilities may be payable from the U.S. Treasury. For legal contingency matters where DLA Counsel is unable to express an opinion regarding the likely outcome of the case and an estimate of the potential legal liability cannot be made, the total amount claimed against the government is classified as "Reasonably Possible" and disclosed if available.

(Refer to Note 1.C., Departures from U.S. GAAP, related to Environmental and Disposal Liabilities and Commitments and Contingencies; Note 10, *Other Liabilities;* Note 11, *Environmental and Disposal Liabilities;* and Note 12, *Commitments and Contingencies.*)

## O. Liabilities

Liabilities represent probable and measurable future outflows of resources as a result of past transactions or events and are recognized when incurred, regardless of whether there are budgetary resources available to pay the liabilities. However, liabilities cannot be liquidated without legislation providing resources and legal authority.

**Liabilities Covered and not Covered by Budgetary Resources:** Liabilities covered by budgetary resources include those liabilities for which Congress appropriated funds and are otherwise available to pay amounts due as of the Balance Sheet dates. Liabilities not covered by budgetary resources are amounts owed in excess of available, congressionally appropriated funds and, therefore, no budgetary resources are available to pay amounts due as of the Balance Sheet dates but will require future funding to liquidate the obligation. (Refer to Note 8, *Liabilities Not Covered by Budgetary Resources*.)

**Liabilities not Requiring Budgetary Resources:** Liabilities that have not in the past required and will not in the future require the use of budgetary resources are referred to as liabilities not requiring budgetary resources.

**Current and Noncurrent Liabilities:** The DLA WCF discloses its other liabilities between current and noncurrent liabilities in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*. The current liabilities represent liabilities that DLA WCF expects to settle within the 12 months of the Balance Sheet dates. Noncurrent liabilities represent liabilities that DLA WCF does not expect to be settled within the 12 months of the Balance Sheet dates (refer to Note 10, *Other Liabilities*).

**Accounts Payable:** Accounts Payable include amounts owed but not yet paid to Intragovernmental and Other than Intragovernmental entities for goods and services received by DLA WCF. DLA WCF estimates and records accruals when services and goods are performed or received (i.e., MOCAS accrual) related to contract financing and Negative Payable accrual to adjust the timing issues that exist when an invoice is received and posted without a goods receipt. DLA WCF also accrues liabilities incurred at month-end but not yet recorded using data from Third Party Payment Systems, GPCs, various feeder systems, and estimates of costs incurred when goods or services received but not invoiced.

**Advances from Others and Deferred Revenue:** Advances from Others and Deferred Revenue are cash received in advance of goods or services that have not been fully rendered.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders, and Note 8, *Liabilities Not Covered by Budgetary Resources*.)

## P. Environmental and Disposal Liabilities

E&DL are a probable and reasonably estimable future outflow or expenditure of resources that exists as of the financial reporting date for environmental cleanup costs resulting from past transactions or events.

The DLA WCF is responsible for accurate reporting of E&DL and expenses for the real property and/or equipment that it records and reports in its financial statements as assets. DLA identifies and estimates accrued E&DL through its annual cost-to-complete (CTC) process. DLA's accrued E&DL comprises of environmental cleanup costs associated with restoration of environmental sites on real property that it does not own but has received contract authority to execute and manage. These environmental sites may include, but are not limited to, decontamination, decommissioning, site restoration, site monitoring, clean closure of assets, and post-closure costs related to the Agency's operations that result in hazardous waste.

On September 29, 2022, the OUSD(C) issued a *Financial Reporting of Environmental and Disposal Liabilities* memorandum, which concluded that the Military Departments are responsible for reporting the entirety of E&DL associated with real property located on their installations for closure liabilities based on FASAB Interpretation 9, *Cleanup Cost Liabilities Involving Multiple Component Reporting Entities: An Interpretation of SFFAS 5 & SFFAS 6* and the DoD FMR 7000.14-R Volume 4, Chapter 13, *Environmental and Disposal Liabilities*. In FY 2023, DLA jointly signed a Memorandum for Record, with each Military Service acknowledging their responsibility for the reporting of E&DL associated with real property. As such, DLA reversed its asset-driven E&DL in FY 2023. Due to noted deficiencies, DLA is not able to reconcile the population of real property assets that encompass the environmental sites closure and asbestos liabilities.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities and Commitments and Contingencies; Note 1.K., *General Property, Plant and Equipment*; Note 11, *Environmental and Disposal Liabilities*; and Note 12, *Commitments and Contingencies*.)

## Q. Payroll and Annual Leave Accruals

Accrued payroll consists of salaries, wages, and other compensation earned by employees, but not yet disbursed as of the Balance Sheet date. DLA accrues the cost of unused annual leave, including, restored leave, compensatory time, and credit hours as earned and reduces the accrual when leave is taken. The payroll and annual leave accrual liability is accrued based on the latest pay period data for reporting purposes (refer to Note 10, *Other Liabilities*).

## R. Federal Employee Benefits Payable

The FECA (Public Law 103-3) provides income and medical cost protection to covered Federal civilian employees injured on the job, to employees who have incurred work-related occupational diseases, and to beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. The FECA program is administered by the Department of Labor (DOL), which pays valid claims and subsequently seeks reimbursement from DLA WCF for these paid claims. The FECA liability consists of two elements.

The first element, accrued FECA liability, is based on actual future payments for claims paid by DOL but not yet reimbursed by DLA WCF. DLA WCF reimburses DOL for claims as funds are appropriated for this purpose. In general, there is a one to two-year period between payment by DOL and reimbursement to DOL by DLA WCF. As a result, DLA WCF recognizes an intragovernmental liability, not covered by budgetary resources, for the claims paid by DOL that will be reimbursed by DLA. (Refer to Note 8, *Liabilities Not Covered by Budgetary Resources*, and Note 9, *Federal Employee Benefits Payable and Related Other Liabilities*.)

The second element, actuarial FECA liability, is the estimated liability for future payments and is recorded as a liability Other than Intragovernmental, not covered by budgetary resources. The actuarial FECA liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. DOL determines the actuarial FECA liability annually, as of September 30, using an actuarial method that considers historical benefit payment patterns, wage inflation factors, medical inflation factors, and other variables. The projected annual benefit payments are discounted to present value. The methodology for billable projected liabilities includes, among other things: (1) an algorithmic model that relies on individual case characteristics and benefit payments (the FECA Case Reserve Model); and (2) incurred but not reported claims were estimated using historical incurred benefit liabilities and payments. (Refer to Note 8, *Liabilities Not Covered by Budgetary Resources,* and Note 9, *Federal Employee Benefits Payable and Related Other Liabilities*.)

## S. Pension Benefits

Based on the effective Federal government start date, DLA WCF's civilian employees participate in either the Civil Service Retirement System (CSRS), a defined benefit plan, or the Federal Employees Retirement System (FERS), a defined benefit plan and contribution plan. The employee pension benefit is managed at the OUSD level. The measurement of the service cost requires the use of an actuarial cost method and assumptions. OPM administers these benefits and provides the factors that DLA applies to calculate and recognize imputed costs, as reported in its Statements of Net Cost, and a corresponding imputed financing sources in the Statements of Changes in Net Position. DLA WCF is not responsible for and does not report CSRS or FERS assets, accumulated plan benefits, or liabilities applicable to its employees. OPM is responsible for and reports these amounts.

## T. Net Position

Net position is the residual difference between assets and liabilities, and consists of Unexpended Appropriations and Cumulative Results of Operations.

**Unexpended Appropriations:** Unexpended appropriations consist of unobligated and undelivered order balances. Unobligated balances are amounts of remaining budgetary resources available for obligation, which have not been rescinded or withdrawn. Undelivered orders are the amount of obligations incurred for goods and/or services ordered, but not yet received. DLA WCF's unexpended appropriations primarily consist of supplemental appropriations and overseas contingency operations.

**Cumulative Results of Operations:** Cumulative results of operations consist of the net difference since inception between: (1) expenses and losses; (2) revenue and gains; and (3) other financing sources.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Net, Revenue, and Unfilled Customer orders and Accounts Payable, Expenses, and Undelivered Orders, and Note 14, *Statement of Budgetary Resources*)

## U. Revenue and Other Financing Sources

**Exchange and Non-exchange Revenue:** The DLA WCF classifies revenue as either exchange revenue or non-exchange revenue. Exchange revenue arises when DLA WCF provides goods or services to Intragovernmental or Other than Intragovernmental entities in exchange for inflows of resources. Exchange revenue is presented in the Statements of Net Cost and serves to offset the costs of these goods and services.

The DLA WCF activities recognize exchange revenue from the sale of petroleum products from DLA Energy, weapon system repair parts from DLA Aviation and DLA Land and Maritime, food and medical supplies from DLA Troop Support, DLA Disposition Services sells eligible DoD excess personal property or its residual materials from disposal operations, or from the reimbursements for goods and services provided to other DoD activities, other Federal agencies and the public. DLA Distribution provides storage and distribution solutions/management, transportation planning/management and logistics planning and contingency operations. The sale of materials includes DLA WCF's Direct sales and Customer Direct sales. DLA WCF's Direct sales are from DLA WCF stock to the customer, whereas Customer Direct sales are from the vendor directly to the customer.

Non-exchange revenue is derived from the government's sovereign right to demand payment, such as specifically identifiable, legally enforceable claims. DLA WCF non-exchange revenue includes interest penalties and administrative fees. Non-exchange revenue is considered to reduce the cost of DLA WCF's operations and is reported in the Statements of Changes in Net Position as a financing source.

DLA Energy Standard Fuel Price: The DLA WCF uses a Standard Fuel Price (SFP) per barrel of fuel sold to customers to include DoD, U.S. Coast Guard, and Foreign Governments.

DLA WCF is responsible for recommending a SFP to OUSD(C). In the process of determining the recommended SFP, DLA WCF considers the amount necessary to recover the cost of the products and services. Upon receiving DLA WCF's proposed SFP, OUSD(C) performs an evaluation of the proposed SFP and determines the final SFP that DLA WCF is required to use for DLA WCF Energy sales.

OUSD(C) sets the final SFP based on OMB derived product assumptions and approved non-product costs for DLA Energy. Based on OUSD(C) direction, the following SFPs were set during FY 2023:

| Effective Date | SFP per Barrel |
|---|---|
| October 1, 2022 | $173.46 |
| February 1, 2023 | $163.80 |

**Steady Support**

Sailors use a guide line to steady a joint light tactical vehicle heavy gun carrier onto an Improved Navy Lighterage System during Resolute Dragon at Kushiro Port, Japan, Oct. 5, 2022. The exercise is designed to strengthen the defensive capabilities of the U.S.-Japan alliance. **Photo By:** Marine Corps Cpl. Alpha Hernandez

DLA WCF was able to recover the full costs of the goods and services provided by DLA Energy during the year ended September 30, 2023, but unable to recover these costs for the year ended September 30, 2022.

DLA Energy Cost Plus: Federal civilian agencies and other authorized customers are charged cost plus as follows, (1) for Customer Direct sales, customers are charged the acquisition cost of fuel billed to DLA Energy by the vendor on the day of delivery plus the cost-plus rate; and (2) for DLA Direct Sales, customers are charged the average acquisition cost of fuel plus the cost-plus rate. The cost-plus rate for FY 2023 is $0.07 cents per gallon. The cost-plus rate for FY 2022 was $0.065 cents per gallon.

Supply Chain Cost Recovery Rate: The DLA WCF establishes the selling price in two separate methods depending on the type of items. For non-National Stock Numbers (NSNs), which include part numbers, local stock numbers or service materials as described in a vendor's product catalog or contract solicitation that a customer can order, the selling price is based on latest acquisition cost plus a CRR. The latest acquisition cost is the cost of acquiring the goods and services. The CRR is a percentage added to the acquisition cost that allows DLA WCF to recover the full cost of the goods and services provided, including depreciation of capital assets, in accordance with U.S. Code Title 10, § 2208.

For NSNs, a standard price is established annually. The selling price is based on the average acquisition cost over the course of the previous twelve months, other material cost (testing, transportation, etc.) and the CRR.

Other Financing Sources: Other financing sources, other than exchange and non-exchange revenue, include additional inflows of resources that increase results of operations during the reporting period. DLA WCF's other financing sources come from unexpended appropriation transfers-in and non-expenditure transfers-in initiated by OUSD, and are recognized as financing sources when used. Other financing sources also include: (1) transfers-in/out without reimbursement; and (2) imputed financing with respect to costs subsidized by another Federal entity.

Transfers-In/Out Without Reimbursement: Transfers-in/out without reimbursement include intragovernmental transfers of capitalized assets. The amount of the transfer is the book value of the transferring entity and if the book value is not known, the amount is the estimated fair value at the date of transfer.

Imputed Financing and Imputed Cost: In certain cases, DLA WCF receives goods and services from other Federal entities at no cost or at a cost less than the full cost to the providing entity. Consistent with accounting standards, certain costs of the providing entity that are not fully reimbursed by DLA WCF are recognized as imputed cost in the Statements of Net Cost and are offset by imputed financing in the Statements of Changes in Net Position. DLA WCF recognizes the following imputed cost and related imputed financing: (1) employee benefits administered by the OPM (i.e., retirement, health, life insurance benefits); and (2) claims settled by the Treasury Judgment Fund. In accordance with SFFAS 55, *Amending Inter-Entity Costs Provisions*, unreimbursed costs of goods and services other than those identified above are not included in DLA WCF financial statements.

(Refer to Note 1.C., *Departures from U.S. GAAP,* related to Accounts Receivable, Net; Revenue, and Unfilled Customer Orders and Inventory and Related Property, Net; Note 4, *Accounts Receivable, Net*; Note 6, *Inventory and Related Property, Net;* and Note 13, *Exchange Revenue.*)

## V. Expenses

Expenses are recognized when there are outflows, usage of assets, or incurrences of liabilities (or a combination) from carrying out functions related to DLA WCF's activity groups, for which benefits do not extend beyond the present operating period. For financial reporting purposes, operating expenses are recognized in the period incurred (refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders).

## W. Transactions with Foreign Governments and International Organizations

The DLA WCF sells defense articles and services to foreign governments and international organizations. Foreign Military Sales (FMS) are governed under the provisions of the Arms Export Control Act of 1976.

DLA Energy enters into fuel supply and services transactions with foreign governments in accordance with DoD Directives 5530.3 and 2010.9, under international agreement statutory authorities. FEA and Direct Bills are governed under the provisions of Acquisition Cross Servicing Agreements or Title 10 Section 2922 (e). The FEAs are international acquisition and cross-servicing agreements established between DLA and the Military Departments of other nations. DLA Energy 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. For FEA transactions, settlement occurs on a periodic basis as prescribed in the FEA. Upon settlement with the foreign country, the purchases of fuel from foreign governments net against sales to the foreign government. Settlement can be made either in fuel or cash. Settlement in fuel is based on the agreed upon price. For cash settlements, the agreements typically call for reciprocal pricing (i.e., prices cannot be more than the participants charge their military service components). Payment for fuel after offsetting quantities is based on a quantity and a price and is an arms-length transaction. Foreign governments with an Acquisition Cross Servicing Agreement and no FEA are Direct Bills and are settled in cash.

DLA Aviation, DLA Distribution, DLA Energy, DLA Troop Support and DLA Land & Maritime support FMS by working directly with Military Departments to fulfill orders for FMS customers. In these cases, the respective Military Department acts as the implementing agency, and not DLA.

DLA Disposition Services conducts the sale of excess defense articles to authorized foreign governments. Property is issued free to grant aid eligible countries and for the adjusted present value for non-grant aid eligible countries. All FMS customers are charged for packing, crating and handling. DLA Disposition Services is reimbursed for administration costs only. This program is overseen and reported by the Defense Security Cooperation Agency (DSCA).

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Net, Revenue, and Unfilled Customer Orders; and Accounts Payable, Expenses, and Undelivered Orders.)

# Note 2: Non-Entity Assets (Unaudited)

Non-Entity Assets as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Other than Intragovernmental** | | |
| Accounts Receivable, Net | $ 5 | $ 4,377 |
| **Total Other than Intragovernmental Assets** | **5** | **4,377** |
| **Total Non-Entity Assets** | **5** | **4,377** |
| **Total Entity Assets** | **32,954,882** | **31,857,343** |
| **Total Assets** | **$ 32,954,887** | **$ 31,861,720** |

Non-Entity Accounts Receivable, Net consists of administrative fees, interest, and penalties and fine receivables.

**Marines on a Mission**

Marines walk to a chemical weapons site during a joint explosive ordnance disposal exercise at Marine Corps Training Area Bellows, Hawaii, Sept. 21, 2022. **Photo by:** Marine Corps Cpl. Patrick King

# Note 3: Fund Balance with Treasury (Unaudited)

Fund Balance with Treasury as of September 30, 2023 and 2022, respectively, consists of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Status of Fund Balance with Treasury** | | |
| Unobligated Balance: | | |
| Available | $ 421,018 | $ 1,081,109 |
| Obligated Balances Not Yet Disbursed | 4,681,400 | 3,621,833 |
| **Total Fund Balance with Treasury** | **$ 5,102,418** | **$ 4,702,942** |

**Status of Fund Balance with Treasury** presents the budgetary and proprietary resources that constitute DLA WCF FBwT. It consists of unobligated and obligated balances. Unobligated and obligated balances differ from the related amounts reported in the Combined Statements of Budgetary Resources because budgetary balances are supported by amounts other than FBwT (e.g., contract authority and budgetary receivables).

**Unobligated Balance - Available** represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations and can be used for future obligations.

**Unobligated Balance - Unavailable** includes the cumulative amount of budget authority and funds not available for obligation from offsetting collections. As of September 30, 2023 and 2022, DLA WCF does not have unobligated unavailable balances.

**Obligated Balance Not Yet Disbursed** represents funds that have been obligated for goods and services not received, and those received but not paid. This balance includes $143.0 million related to an accounts payable pending litigation. For FY 2021, the noted funds were included in the deposit accounts as part of DoD consolidated financial statements and reported as an accounts receivable in DLA financial statements.

**Non-budgetary FBwT** consists of FBwT in unavailable receipt accounts and clearing accounts that do not have budget authority and non-budgetary FBwT such as non-fiduciary deposit funds. As of September 30, 2023 and 2022, DLA WCF does not have non-budgetary FBwT.

**Other Information** includes the following tables summarizing the undistributed collections and disbursements between U.S. Treasury and DLA WCF as of September 30, 2023 and 2022, respectively:

| FY 2023 Adjustments of Undistributed Collections and Disbursements (dollars in thousands) | | | |
|---|---|---|---|
| **Transaction Type** | **Treasury Balance based on CMR** | **DLA WCF Trial Balance** | **Balances Not Yet Recorded in DLA Accounting System - Undistributed** |
| Collections | $ 44,925,246 | $ 45,064,948 | $ (139,702) |
| Disbursements | $ 44,998,406 | $ 44,938,171 | $ 60,235 |

| FY 2022 Adjustments of Undistributed Collections and Disbursements (dollars in thousands) | | | |
|---|---|---|---|
| **Transaction Type** | **Treasury Balance based on CMR** | **DLA WCF Trial Balance** | **Balances Not Yet Recorded in DLA Accounting System - Undistributed** |
| Collections | $ 43,107,778 | $ 42,843,452 | $ 264,326 |
| Disbursements | $ 43,878,715 | $ 43,681,368 | $ 197,347 |

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Fund Balance with Treasury.)

# Note 4: Accounts Receivable, Net (Unaudited)

Accounts Receivable, Net as of September 30, 2023 and 2022, respectively, consists of the following (dollars in thousands):

| FY 2023 | | | |
|---|---|---|---|
| | Accounts Receivable | (Less: Allowance for Doubtful Accounts) | Accounts Receivable, Net |
| **Intragovernmental Accounts Receivable, Net** | | | |
| Energy | $ 300,896 | $ (4,849) | $ 296,047 |
| Supply Chain Management | 1,833,261 | (218,902) | 1,614,359 |
| Document Services | 44,339 | (10,752) | 33,587 |
| **Total Intragovernmental Accounts Receivable, Net** | **$ 2,178,496** | **$ (234,503)** | **$ 1,943,993** |
| **Other than Intragovernmental Accounts Receivable, Net** | | | |
| Energy | $ 596,559 | $ (32,262) | $ 564,297 |
| Supply Chain Management | 390,952 | (36,032) | 354,920 |
| Document Services | 1,725 | (32) | 1,693 |
| **Total Other than Intragovernmental Accounts Receivable, Net** | **$ 989,236** | **$ (68,326)** | **$ 920,910** |

| FY 2022 | | | |
|---|---|---|---|
| | Accounts Receivable | (Less: Allowance for Doubtful Accounts) | Accounts Receivable, Net |
| **Intragovernmental Accounts Receivable, Net** | | | |
| Energy | $ 250,127 | $ (1,998) | $ 248,129 |
| Supply Chain Management | 1,410,273 | (140,434) | 1,269,839 |
| Document Services | 36,952 | (9,636) | 27,316 |
| **Total Intragovernmental Accounts Receivable, Net** | **$ 1,697,352** | **$ (152,068)** | **$ 1,545,284** |
| **Other than Intragovernmental Accounts Receivable, Net** | | | |
| Energy | $ 425,813 | $ (35,961) | $ 389,852 |
| Supply Chain Management | 362,486 | (27,610) | 334,876 |
| Document Services | 1,185 | (24) | 1,161 |
| **Total Other than Intragovernmental Accounts Receivable, Net** | **$ 789,484** | **$ (63,595)** | **$ 725,889** |

Of the Total Other than Intragovernmental Accounts Receivable, Net, criminal restitutions, net consist of $81.1 million and $7.5 million, as of September 30, 2023 and 2022, respectively. The gross amount of criminal restitutions consists of $91.9 million and $11.6 million with a related allowance of doubtful accounts of $10.8 million and $4.1 million as of September 30, 2023 and 2022, respectively.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Net, Revenue, and Unfilled Customer Orders.)

# Note 5: Other Assets (Unaudited)

Other Assets as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Intragovernmental Other Assets** | | |
| Other Assets | $ 123,306 | $ 123,306 |
| **Total Intragovernmental Other Assets** | **123,306** | **123,306** |
| **Total Other Assets** | **$ 123,306** | **$ 123,306** |

**Intragovernmental Other Assets** consist of Strategic Petroleum Reserve for National Defense purposes. This includes crude oil held by the DoE on behalf of the DoD. The Strategic Petroleum Reserve is valued at historical acquisition cost.

# Note 6: Inventory and Related Property, Net (Unaudited)

Inventory and Related Property, Net as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | Valuation Method | FY 2023 | FY 2022 |
|---|---|---|---|
| **Inventory Categories:** | | | |
| Held for Sale | MAC | $ 23,581,726 | $ 23,562,928 |
| Reserved for Future Sale | MAC | 292,998 | 259,727 |
| Held for Repair | MAC | 112,554 | 110,693 |
| Less: Allowance for Repairs | | (2,251) | (2,214) |
| **Total Inventory and Related Property, Net** | | **$ 23,985,027** | **$ 23.931,134** |

**MAC** = Moving Average Cost

As of September, 30, 2023 and 2022, DLA SCM is holding $126.2 million and $107.2 million, respectively, of inventory not available for sale due to litigation.

All inventory identified as EOU has an expected NRV of zero as of September 30, 2023 and 2022.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Inter-Entity Cost and Inventory and Related Property, Net.)

# Note 7: General Property, Plant and Equipment, Net (Unaudited)

General Property, Plant and Equipment, Net as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | Acquisition Value | Accumulated Depreciation/ Amortization | Net Book Value |
|---|---|---|---|
| **Major Asset Classes:** | | | |
| Internal-Use Software | $ 776,068 | $ (710,818) | $ 65,250 |
| General Equipment | 445,102 | (379,367) | 65,735 |
| Internal-Use Software in Development | 45,647 | - | 45,647 |
| Construction-in-Progress | 599,124 | - | 599,124 |
| **Total General PP&E, Net** | **$ 1,865,941** | **$ (1,090,185)** | **$ 775,756** |

| FY 2022 | Acquisition Value | Accumulated Depreciation/ Amortization | Net Book Value |
|---|---|---|---|
| **Major Asset Classes:** | | | |
| Internal-Use Software | $ 718,685 | $ (687,784) | $ 30,901 |
| General Equipment | 401,479 | (344,806) | 56,673 |
| Internal-Use Software in Development | 67,726 | - | 67,726 |
| Construction-in-Progress | 583,562 | - | 583,562 |
| **Total General PP&E, Net** | **$ 1,771,452** | **$ (1,032,590)** | **$ 738,862** |

Software primarily consists of e-Procurement software, Risk Based Inspection software, and DAI software. General Equipment primarily consists of fuel handling systems, conveyor systems, scrap shredders, and electronic security systems.

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The table below discloses activity for General Property, Plant and Equipment, Net as of September 30, 2023 and 2022, respectively (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **General PP&E, Net - Beginning Balances** | **$ 738,862** | **$ 810,370** |
| Capitalized Acquisitions | 139,859 | 125,508 |
| Dispositions | (31,491) | (6,306) |
| Depreciation | (68,704) | (61,188) |
| Transfers in/out without reimbursements | (2,770) | (129,522) |
| **General PP&E, Net - Ending Balances** | **$ 775,756** | **$ 738,862** |

Effective FY 2020, DoD's policy regarding real property is that it must be reported in the financial statements of the military service that is the Installation Host having jurisdiction of the real property asset.

In FY 2023, DLA WCF transferred 43 real property assets in the amount of $144.1 million to the military services. This amount consisted of an acquisition value and accumulated depreciation of $149.4 million and $5.3 million, respectively. In FY 2022, DLA WCF transferred 92 real property assets in the amount of $298.6 million to the military services. This amount consisted of an acquisition value and accumulated depreciation of $315.8 million and $17.2 million, respectively.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to General Property, Plant and Equipment, Net, and Leases.)

**Drone Training**

Marine Corps Lance Cpl. Donte Mathews flies an unmanned aircraft system during a mortar range event at Camp Lejeune, N.C., Jan. 17, 2023. **Photo by:** Marine Corps Cpl. Michael Virtue

# Note 8: Liabilities Not Covered by Budgetary Resources (Unaudited)

Liabilities Not Covered by Budgetary Resources as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Intragovernmental Liabilities** | | |
| Other Liabilities - Benefits Program Contributions Payable | $ 19,031 | $ 14,999 |
| Other Liabilities | - | 870 |
| **Total Intragovernmental Liabilities** | **19,031** | **15,869** |
| | | |
| **Other than Intragovernmental Liabilities** | | |
| Environmental and Disposal Liabilities | 210,895 | 1,085,673 |
| Federal Employee Benefits Payable | 195,840 | 148,883 |
| Other Liabilities | 801 | 189 |
| **Total Other than Intragovernmental Liabilities** | **407,536** | **1,234,745** |
| **Total Liabilities Not Covered by Budgetary Resources** | **426,567** | **1,250,614** |
| **Total Liabilities Covered by Budgetary Resources** | **4,151,106** | **4,564,176** |
| **Total Liabilities Not Requiring Budgetary Resources** | **5** | **4,377** |
| **Total Liabilities** | **$ 4,577,678** | **$ 5,819,167** |

**Other Liabilities - Benefits Program Contributions Payable (Intragovernmental)** consist of unfunded accrued FECA liability based on DOL records.

**Other Liabilities (Intragovernmental)** represent Judgment Fund liabilities. DLA is required to reimburse Treasury for the litigative and administrative payments/settlements made on behalf of DLA pursuant to the Contract Disputes Act and the Notification and Federal Employee Anti-discrimination and Retaliation Act of 2002 (No FEAR Act).

**Environmental and Disposal Liabilities (Other than Intragovernmental)** consist of probable and reasonably estimable future outflow or expenditure of resources that exist as of the financial reporting date for environmental cleanup costs resulting from past transactions or events. As of September 30, 2023, and 2022, the total liabilities covered by budgetary resources for the E&DL consist of $124.2 million and $148.1 million, respectively.

**Federal Employee Benefits Payable (Other than Intragovernmental)** are comprised of FECA actuarial liability based on DOL records.

**Other Liabilities (Other than Intragovernmental)** are comprised of contingent legal liabilities.

**Liabilities Not Requiring Budgetary Resources** consist of custodial activity related to taxes/fees collected from the sale of fuel, etc. that will be transferred to Treasury, which do not require budgetary resources.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders; and Commitments and Contingencies; Note 9, F*ederal Employee Benefits Payable and Related Other Liabilities*; Note 11, *Environmental and Disposal Liabilities*, and Note 12, *Commitments and Contingencies*.)

# Note 9: Federal Employee Benefits Payable and Related Other Liabilities (Unaudited)

Federal Employee Benefits Payable and Related Other Liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | Liabilities | (Less: Assets Available to Pay Benefits) | Unfunded Liabilities |
|---|---|---|---|
| **Intragovernmental Other Liabilities** | | | |
| Employer Contributions and Payroll Taxes Payable | $ 19,581 | $ (19,581) | $ - |
| Unfunded FECA Liability | 19,031 | - | 19,031 |
| Other Post Employment Benefits Due and Payable | 1,453 | (1,453) | - |
| **Total Intragovernmental Other Liabilities** | **$ 40,065** | **$ (21,034)** | **$ 19,031** |
| **Other than Intragovernmental Federal Employee Benefits Payable** | | | |
| Actuarial FECA Liability | $ 195,840 | $ - | $ 195,840 |
| Employer Contributions and Payroll Taxes Payable | 26,234 | (26,234) | - |
| **Total Other than Intragovernmental Federal Employee Benefits Payable** | **$ 222,074** | **$ (26,234)** | **$ 195,840** |

| FY 2022 | Liabilities | (Less: Assets Available to Pay Benefits) | Unfunded Liabilities |
|---|---|---|---|
| **Intragovernmental Other Liabilities** | | | |
| Employer Contributions and Payroll Taxes Payable | $ 19,523 | $ (19,523) | $ - |
| Unfunded FECA Liability | 17,790 | (2,791) | 14,999 |
| Other Post Employment Benefits Due and Payable | 2,245 | (2,245) | - |
| **Total Intragovernmental Other Liabilities** | **$ 39,558** | **$ (24,559)** | **$ 14,999** |
| **Other than Intragovernmental Federal Employee Benefits Payable** | | | |
| Actuarial FECA Liability | $ 148,883 | - | $ 148,883 |
| Employer Contributions and Payroll Taxes Payable | - | - | - |
| **Total Other than Intragovernmental Federal Employee Benefits Payable** | **$ 148,883** | **$ -** | **$ 148,883** |

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**Employer Contributions and Payroll Taxes Payable** are the employer portion of payroll taxes and benefit contributions for health benefits, retirement, life insurance and voluntary separation incentive payments.

**Unfunded FECA Liability (Intragovernmental)** includes the accrued FECA liability paid by DOL but not yet reimbursed by DLA WCF.

**Other Post-Employment Benefits Due and Payable (Intragovernmental)** consist of amounts due to former or inactive employees (not retired) and/or beneficiaries.

**Actuarial FECA Liability (Other than Intragovernmental)** is workers' compensation benefits developed by the DOL Office of Workers' Compensation Programs and provided to DLA WCF at the end of each FY. 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 OMB's 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.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders.)


**Delivery Drivers**

Sailors aboard the aircraft carrier USS George H.W. Bush wait to move supplies during a replenishment with the fast combat support ship USNS Arctic in the Ionian Sea, Jan. 22, 2023. **Photo by:** Navy Petty Officer 3rd Class Nicholas Avis

# Note 10: Other Liabilities (Unaudited)

Other Liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | Current | Non-Current | Total |
|---|---|---|---|
| **Intragovernmental Other Liabilities** | | | |
| Custodial Liabilities | $ 5 | $ - | $ 5 |
| Other Liabilities | - | - | - |
| **Total Intragovernmental Other Liabilities** | **$ 5** | **$ -** | **$ 5** |
| **Other than Intragovernmental Other Liabilities** | | | |
| Accrued Funded Payroll and Benefits | $ 304,507 | $ - | $ 304,507 |
| Contract Holdbacks | - | 888 | 888 |
| Contingent Liabilities | 801 | - | 801 |
| **Total Other than Intragovernmental Other Liabilities** | **$ 305,308** | **$ 888** | **$ 306,196** |

| FY 2022 | Current | Non-Current | Total |
|---|---|---|---|
| **Intragovernmental Other Liabilities** | | | |
| Custodial Liabilities | $ 4,377 | $ - | $ 4,377 |
| Other Liabilities | 870 | - | 870 |
| **Total Intragovernmental Other Liabilities** | **$ 5,247** | **$ -** | **$ 5,247** |
| **Other than Intragovernmental Other Liabilities** | | | |
| Accrued Funded Payroll and Benefits | $ 323,018 | $ - | $ 323,018 |
| Contract Holdbacks | - | (3) | (3) |
| Contingent Liabilities | 189 | - | 189 |
| **Total Other than Intragovernmental Other Liabilities** | **$ 323,207** | **$ (3)** | **$ 323,204** |

**Custodial Liabilities (Intragovernmental)** are liabilities for collections reported as non-exchange revenues where DLA is acting on behalf of another Federal entity. (Refer to Note 2, *Non-Entity Assets*.)

**Other Liabilities (Intragovernmental)** represent U.S. Treasury Judgment Fund liabilities. DLA is required to reimburse Treasury for the litigative, and administrative payments/settlements made on behalf of DLA pursuant to the Contract Disputes Act and the No FEAR Act.

**Accrued Funded Payroll and Benefits (Other than Intragovernmental)** include salaries, wages, leave, and other compensation earned by employees but not yet disbursed.

**Contract Holdbacks (Other than Intragovernmental)** are amounts earned by contractors or suppliers during the production period but not yet paid to the contractor/supplier to ensure future performance.

**Contingent Liabilities (Other than Intragovernmental)** are a loss determined to be probable and the amount is estimable based on the outcome of an uncertain future event. The current portion is contingencies related to litigation (refer to Note 12, *Commitments and Contingencies*).

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders; and Commitments and Contingencies, and Note 12, *Commitments and Contingencies*.)

# Note 11: Environmental and Disposal Liabilities (Unaudited)

Environmental and Disposal Liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Environmental and Disposal Liabilities** | | |
| Other Accrued Environmental Liabilities - Non-BRAC: | | |
| Environmental Corrective Action | $ 335,068 | $ 366,218 |
| Environmental Closure Requirements | - | 865,816 |
| Asbestos | - | 1,753 |
| **Total Environmental and Disposal Liabilities** | **$ 335,068** | **$ 1,233,787** |

The DLA WCF E&DL are comprised of two primary elements: (1) existing obligations supporting the Defense WCF environmental restoration programs, and (2) the Cost to Complete (CTC) which includes anticipated future costs necessary to complete the environmental restoration requirements at DLA Energy and Non-Energy environmental restoration sites.

In FY 2023 and FY 2022, DLA WCF utilized the Remedial Action Cost Engineering and Requirements (RACER) software to generate the CTC estimates of anticipated future costs. DLA WCF includes E&DL for environmental corrective action sites under both DLA Energy and Non-Energy management.

As of September 30, 2023, and 2022, the total E&DL consist of $335.1 million and $1.2 billion, respectively.

FY 2023 cost estimates under DLA Energy management and Non-Energy management were generated for sites with environmental corrective action costs.

Per DoD policy and FASAB guidance, Military Departments are responsible for reporting the entirety of E&DL associated with real property located on their installations for Environmental Closure Requirements and Asbestos E&DL. Accordingly, as of September 30, 2023, DLA WCF has no reportable Environmental Closure Requirements and Asbestos E&DL.

**Types of Environmental Liabilities and Disposal Liabilities:** The DLA WCF is responsible for the recognition, measurement, reporting, and disclosure of Non-BRAC E&DL. Non-BRAC E&DL are specifically related to past and current installation restoration activities and operations. All clean-up and disposal actions are conducted in coordination with regulatory agencies, other responsible parties, and current property owners.

The DLA WCF reportable E&DL is under Other Accrued E&DL – Non-BRAC and includes the following line item:

Environmental Corrective Action: E&DL associated with the cleanup sites not eligible for DERP funding, typically conducted under Resource Conservation and Recovery Act (RCRA) or other Federal or state statutes and regulations.

The DLA WCF assessed its real property and General Equipment inventories and does not currently have reportable WCF E&DL for Environmental Closure Requirements, Asbestos, or General Equipment.

Beginning in FY 2023, DLA fully reduced its recognized WCF Environmental Closure Requirements and Asbestos E&DL balances to zero, in accordance with the September 2022 OUSD(C) memorandum clarifying that installation hosts are responsible for recognizing E&DL related to real property assets regardless of which entity funds and executes the closure activities.

There are no other reportable E&DL categories as listed on the DoD 7000.14-R Financial Management Regulation (FMR) Volume 6B, Chapter 10 – *Note to the Financial Statements, Paragraph 1017, Figure 10-31. Environmental and Disposal Liabilities* (February 2023).

**Applicable Laws and Regulations for Cleanup Requirements:** The DLA WCF 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. DLA WCF is required to comply with the following laws and regulations for Corrective Actions, where applicable: The Comprehensive Environmental Response, Compensation, and Liability Act; the Superfund Amendments and Reauthorization Act; RCRA; and other applicable Federal, State, and local laws and regulations. Required cleanup may at times extend beyond Installation boundaries onto privately owned property or onto sites where DLA WCF is named as a potentially responsible party by a regulatory agency. DLA WCF reports corrective action related E&DL in accordance with SFFAS 5: *Accounting for Liabilities of the Federal Government* and Federal Financial Accounting and Auditing Technical Release 2: *Determining Probable and Reasonably Estimable for Environmental Liabilities in the Federal Government*.

The DLA WCF is no longer required to report asset related E&DL for assets it is not reporting on its financial statements due to policy changes to the DoD 7000.14-R FMR Volume 4 Chapter 13 – *Environmental and Disposal Liabilities* (March 2022), FASAB Interpretation of Federal Financial Accounting Standards 9, *Cleanup Cost Liabilities Involving Multiple Component Reporting Entities: An Interpretation of SFFAS 5 & SFFAS 6*, and the resulting September 2022 OUSD(C) memorandum clarifying that installation hosts are responsible for recognizing E&DL related to real property assets regardless of which entity funds and executes the closure activities. Following issuance of the OUSD(C) Memorandum, in FY 2023 DLA coordinated with, and formally notified, each Service with the intent to no longer report E&DL related to assets located on other Services' installations via signed memorandums.

**Methods for Assigning Estimated Total Cleanup Costs to Current Operating Periods:** To estimate future environmental costs, DLA WCF utilizes a combination of historical or pre-negotiated contract costs, proposal costs, engineering estimates, and in the absence of other detailed information, parametric estimates created using the RACER software. Any historical costs used in the creation of the estimates for DLA WCF E&DL are adjusted for inflation and reported in current year dollars. The RACER Steering Committee ensures that the RACER software is Validated, Verified, and Accredited (VV&A) in accordance with DoD Instruction 5000.61– DoD Modeling and Simulation (M&S) Verification, Validation, and Accreditation. The DoD is working with the RACER Steering Committee and stakeholders to identify improvements to RACER functionality, auditability, and documentation.

**Nature of Estimates and the Disclosure of Information Regarding Possible Changes Due to Inflation, Deflation, Technology, or Applicable Laws and Regulations:** The DLA E&DL Site Identification (ID) process tracks environmental events such as spills and releases in an Environmental Event Repository and evaluates each event annually for E&DL potentiality to determine the annual CTC inventory. DLA WCF E&DL estimates are created annually for all projected requirements and are finalized and approved by July. The estimates are then reevaluated through a roll forward review to identify any material changes to previously approved estimates to ensure accuracy as of the financial reporting date of September 30. Processes are conducted in accordance with DLA ELM SOPs and the DoD 7000.14-R FMR Volume 4, Chapter 13 – *Environmental and Disposal Liabilities* (March 2022).

CTC estimates revised through roll forward, as applicable, and prior year obligations are reported in the balance as of September 30. As of the reporting date, material changes to approved CTC estimates for two sites were identified through the roll forward review. In accordance with the roll forward process, costs for these two sites were recalculated to capture the changes, and revised costs are reflected in the Environmental Corrective Action E&DL balance stated above.

Beginning in FY 2023, DLA fully reduced its WCF recognized Environmental Closure Requirements and Asbestos E&DL balances to zero, in accordance with the September 2022 OUSD(C) memorandum clarifying that installation hosts are responsible for recognizing E&DL related to real property assets regardless of which entity funds and executes the closure activities. In addition, DLA WCF is not aware of any other changes to estimates that would result from inflation, deflation, technology, plans, and/or pending changes to applicable laws and regulations. The cost estimate changes from prior periods are primarily driven by remediation activities and operations, as evidenced by UDOs; there are minor adjustments for inflation or other similar administrative costs throughout the fiscal year. E&DL estimates are reevaluated each year and may change in the future due to changes in laws and regulations, changes in agreements with regulatory agencies, and advances in technology.

**Uncertainty Regarding the Accounting Estimates Used to Calculate the Reported Environmental and Disposal Liabilities:** The stated total WCF E&DL includes prior year obligations and the estimate of future costs necessary to complete requirements. DLA WCF has instituted extensive controls to ensure that these estimates are accurate and reproducible. The cost estimates produced through the ELM process are considered accounting estimates, which require certain judgments and assumptions that are reasonable based upon information available at the time the estimates are calculated. Actual costs may materially vary from the accounting estimates if agreements with regulatory agencies require remediation or closure activities to a different degree than anticipated when calculating the estimates. WCF E&DL can be further affected if investigation of the environmental sites reveals contamination levels that differ from the estimated parameters.

DLA utilizes a formalized Site ID process to identify, track, and evaluate environmental events where the potential for an out-year E&DL exists but the E&DL is not probable and measurable. These environmental events will be re-evaluated in the following fiscal year to determine if any changes have taken place and sufficient information/data is available to create an estimate of future costs that would be included in the Environmental Corrective Action E&DL balance.

## Red Hill Bulk Fuel Storage Tank Facility

The Red Hill Underground Bulk Fuel Storage Tank Facility is located on the Island of Oahu, Hawaii, and consists of twenty steel-lined concreted tanks encased in concrete built into cavities mined inside Red Hill during the period immediately preceding World War II.

On November 20, 2021, an incident occurred in which fuel was released into the environment and migrated into the Red Hill well, contaminating the water supply for Joint Base Pearl Harbor Hickam. On August 31, 2022, the DoD issued a Report on Red Hill Response Cost Projections to inform Congress of DoD's known and projected costs to defuel and permanently close the storage tank facility to comply with the State of Hawaii Department of Health (DOH) order and protect the health and safety of the local population. The cost projections to date reflect ongoing DoD conferrals with the Hawaii Department of Health and the Environmental Protection Agency. The complete array of associated closure requirements and parameters for the Facility will not be known until full defueling has been completed, which is not expected until June 2024. Identification of all remediation requirements will continue beyond that point.

As of September 30, 2023, the DoD-wide known projected costs to defuel and permanently close the Red Hill Fuel Storage Facility total $2.0 billion, as documented in the "Department of Defense Report on Red Hill Response Cost Projections", dated August 31, 2022. Of this amount, DLA's projected cost is $1.4 billion to restore access to safe water, support for families, emergency defueling and fuel dispersal. For the years ended September 30, 2023 and 2022, DLA obligated $764.3 million and $112.0 million, respectively. As these costs to date reflect operational closure activities and not environmental remediation costs, these costs spent to date are not E&DL. Environmental Corrective Actions required to clean up prior petroleum releases (event-driven liability) at the Red Hill facility are currently unknown. Response to the 2021 incident will continue to be tracked as a Potential Out-Year E&DL until environmental investigations have been completed and a path forward to obtain regulatory closure of the facility can be determined. The Department of the Navy is responsible for reporting E&DL associated with Tank Closure, including cleaning of tanks and pipelines, disposal of sludge and waste, tank closure alternatives analysis, and as necessary, infrastructure disposition.

**Unrecognized Costs:** The DLA WCF has no unrecognized costs as there are no reportable Asset-related Environmental Closure Requirements, Asbestos, and General Equipment related E&DL.

**Cleanup Costs Associated with Overseas Environmental Liabilities:** Total overseas cleanup E&DL includes four environmental corrective action sites at three installations across three countries/territories.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities and Commitments and Contingencies; Note 8, *Liabilities Not Covered by Budgetary Resources*; and Note 12, *Commitments and Contingencies.*

# Note 12: Commitments and Contingencies (Unaudited)

Accrued and reasonably possible legal and environmental contingent liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | | | | | | |
|---|---|---|---|---|---|---|
| | | Accrued Liabilities | Estimated Range of Loss | | | |
| | | | Lower End | | Upper End | |
| Legal Contingencies | | | | | | |
| Probable | $ | 801 | $ | 801 | $ | 1,710 |
| Reasonably Possible | | | $ | 33,191 | $ | 551,849 |
| Environmental Contingencies | | | | | | |
| Probable | $ | 335,068 | $ | - | $ | - |
| Reasonably Possible | | | $ | - | $ | - |

| FY 2022 | | | | | | |
|---|---|---|---|---|---|---|
| | | Accrued Liabilities | Estimated Range of Loss | | | |
| | | | Lower End | | Upper End | |
| Legal Contingencies | | | | | | |
| Probable | $ | 189 | $ | 189 | $ | 230 |
| Reasonably Possible | | | $ | 2,227 | $ | 334,204 |
| Environmental Contingencies | | | | | | |
| Probable | $ | 1,233,787 | $ | - | $ | - |
| Reasonably Possible | | | $ | - | $ | - |

**Legal Contingencies:** The DLA WCF is a party in various administrative proceedings and legal actions related to claims for environmental damages, equal opportunity matters, employee or applicant related matters, contract related matters, and contractual bid protests. DLA's Enterprise Workflow Support Capability (EWSC) is used by the Office of General Counsel to report the outcomes and possible liability amounts of open cases.

The DLA WCF did not identify a specific amount within the range of estimated amounts and has accrued the lower end of the range for probable contingent liabilities. Probable contingent liabilities are legal actions where the Office of General Counsel considers an adverse decision probable, and the amount of loss is estimable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the U.S. Treasury Judgment Fund. DLA WCF records contingent liabilities (refer to Note 10, *Other Liabilities*) within Other Liabilities in the Balance Sheets.

Cases for which legal counsel determines an adverse outcome is reasonably possible and the possible financial outflow is measurable, are not recorded, but disclosed as reasonably possible for financial reporting purposes.

Of the 121 legal matters classified as "Reasonably Possible", there are 35 matters where DLA Counsel is unable to express an opinion regarding the likely outcome of the case and an estimate of the potential liability cannot be made. In these 35 matters, the total claimed against the government is $0.6 million.

**Environmental Contingencies:** The DLA WCF has developed a process to identify, estimate, and record contingent E&DL. The WCF does not estimate a potential range of loss in this process. Where DLA WCF is aware of probable and measurable future outflow of resources due to a past event or exchange transaction, the appropriate program categories are reported in Note 11, *Environmental and Disposal Liabilities*.

**Potential Loss Related to Economic Price Clause Contracts:** The DLA WCF is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may result in a future outflow of expenditures. DLA WCF has limited automated system processes by which it captures or assesses these potential liabilities; therefore, the amounts reported may not fairly present DLA WCF's total contingent liabilities. Known contingencies that are considered both measurable and probable have been recognized and recorded as liabilities in the Balance Sheets. DLA WCF does not have contract financing payment contingencies as of September 30, 2023.

**Commitments:** The DLA WCF does not have obligations related to canceled appropriations for contractual commitments.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities; and Commitments and Contingencies, Note 10, *Other Liabilities*; and Note 11, *Environmental and Disposal Liabilities.)*

# Note 13: Exchange Revenue (Unaudited)

The DLA WCF pricing policy for SCM and Energy Management is to seek full cost recovery for products and services provided. These DLA WCF activities maintain the goal to break-even over a single year or two-year period; however, the SCM may request a waiver from the OUSD(C) to recover costs beyond the budget year to maintain a stabilized CRR. DLA WCF establishes its selling or standard prices in the budget to ensure sufficient budgetary resources are available to cover the costs of operations. The prices are normally stabilized or fixed during execution to mitigate the impact of unforeseen fluctuations. DLA WCF will not change the prices during the fiscal year unless prior approval from OUSD(C) is received, except for those instances in which the SCM out-of-cycle price changes may be made without OUSD(C) approval.

The DLA Energy Management generally bills its customers using petroleum standard price mandated by OUSD(C). OUSD(C) establishes the standard price for petroleum and product costs on an annual basis (refer to Note 1.U, *Revenue and Other Financing Sources*, related to non-NSN and cost-plus pricing).

For the years ended September 30, 2023 and 2022, DLA WCF recognized other accounting gains of approximately $1.3.billion and $1.2 billion, respectively, and losses of approximately $1.6 billion and $1.6 billion, respectively, derived from supply chain activities involving MAC updates, receipts without purchase orders, errors due to inventory receipts, NRV updates, and disposal of demilitarized property.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Net, Revenue, and Unfilled Customer Orders; and Inventory and Related Property, Net.)

**Pecan Pie Prep**

Air Force Airman 1st Class Bianca Hrynciw, a services specialist with the 127th Force Support Squadron, prepares dessert for a Thanksgiving-style dinner for members of the 127th Wing at Selfridge Air National Guard Base, Mich., Nov. 5, 2022. **Photo By:** Air Force Tech. Sgt. Samara Taylor, Air National Guard

# Note 14: Statement of Budgetary Resources (Unaudited)

**Unobligated Balance Brought Forward, October 1:** There were no adjustments during the current year to correct the unobligated balance brought forward, October 1. Components of the amount reported as "Unobligated Balance from Prior Year Budget Authority, net" are disclosed in the table below. Other adjustments consist of recoveries of prior year obligated balances, unobligated balance transferred from other accounts and unobligated balance of contract authority withdrawn. The following table displays a reconciliation between the prior year's unobligated balance, end of year amount to the current year's unobligated balance from prior year budget authority, net amount (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Reconciliation of PY Ending Unobligated Balances of CY Beginning Unobligated Balances** | | |
| Unobligated balance brought forward, October 1 | $ 1,081,109 | $ 301,940 |
| Unobligated balance transferred from other accounts | 119,520 | 2,638,927 |
| Adjustment of unobligated balance brought forward, October 1 (+ or -) | | |
| Recoveries of prior year unpaid obligations | 8,931,491 | 6,689,330 |
| Unobligated balance of contract authority withdrawn (-) | (8,920,998) | (6,666,022) |
| Recoveries of prior year paid obligations | - | 541,961 |
| **Unobligated balance, total** | **$ 1,211,122** | **$ 3,506,136** |

**Contract Authority:** Congress intended DLA Energy and DLA SCM to operate in a businesslike manner and to carry out its mission free from the uncertainty inherent in the annual appropriations process. Therefore, Congress has permitted DLA Energy and SCM to enter multiyear contracts.

The amount of contract authority reflected as available in the Combined Statements of Budgetary Resources has increased to $56.8 billion as of September 30, 2023, from $52.4 billion as of September 30, 2022.

**Undelivered Orders (UDOs):** for the years ended September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Intragovernmental Undelivered Orders** | | |
| Unpaid | $ 1,367,053 | $ 2,030,544 |
| **Total Intragovernmental Undelivered Orders** | **1,367,053** | **2,030,544** |
| **Other than Intragovernmental Undelivered Orders** | | |
| Unpaid | 30,167,396 | 25,798,159 |
| Paid | 103,477 | 94,303 |
| **Total Other than Intragovernmental Undelivered Orders** | **30,270,873** | **25,892,462** |
| **Total Undelivered Orders** | **$ 31,637,926** | **$ 27,923,006** |

UDOs represent the amount of goods and/or services ordered to perform DLA WCF's mission objectives that have not been received. Unpaid UDOs represent obligations for goods and services that have not been received or paid. Whereas paid UDOs represent obligations for goods and services that have been paid for in advance of receipt. For the years ended September 30, 2023 and 2022, respectively, DLA WCF does not have Intragovernmental Paid UDO balances.

Due to system limitations, DLA WCF is unable to determine the Intragovernmental and Other than Intragovernmental allocation of UDOs. DLA WCF estimates the allocation of Intragovernmental and Other than Intragovernmental unpaid UDOs based on funded liabilities, excluding payroll and employee benefit liabilities, and paid UDOs based on advances and prepayments reported on the Balance Sheets.

(Refer to Note 1.C., Departures from U.S. GAAP, related to Intragovernmental/Intra-departmental and Other than Intergovernmental Transaction; and Accounts Payable, Expenses, and Undelivered Orders.)

**Contributed Capital:** The DLA WCF received additional funding through the allotment of appropriations from DoD reprogramming actions in the amount of $472.6 million, which consists of $119.5 million of transfers of prior year balances and $353.1 million of current year authority, as of September 30, 2023, and $2.8 billion which consisted of $2.7 billion of transfers of prior year balances and $128.7 million of current year authority, for the year ended September 30, 2022.

### Artisan at Work

It takes a steady hand to sew a flag and Nancy Chhim, a DLA Troop Support Sewing Machine Operator, is a pro at her craft. She's the only person in the world who fringes the U.S. Presidential flag. July 28, 2021. **Photo by** Nutan Chada, DLA Public Affairs

# Note 15: Reconciliation of Net Cost to Net Outlays (Unaudited)

Reconciliation of Net Cost to Net Outlays for the years ended September 30, 2023 and 2022 consist of the following (dollars in thousands):

| FY 2023 | | | |
|---|---|---|---|
| | Intragovernmental | Other than Intragovernmental | Total |
| **NET COST** | **$ (35,295,051)** | **$ 33,702,077** | **$ (1,592,974)** |
| **Components of Net Cost That are Not Part of Net Outlays** | | | |
| General Property, Plant and Equipment Depreciation | - | (68,704) | (68,704) |
| General Property, Plant and Equipment Disposal | - | (31,493) | (31,493) |
| Cost of Goods Sold | (6,374,788) | (29,375,637) | (35,750,425) |
| Net Gains/(Losses) | - | (272,731) | (272,731) |
| **Increase/(Decrease) in Assets:** | | | |
| Accounts Receivable, Net | 398,709 | 195,021 | 593,730 |
| Advances and Prepayments | - | 9,174 | 9,174 |
| **(Increase)/Decrease in Liabilities:** | | | |
| Accounts Payable | 60,211 | (658,926) | (598,715) |
| Environmental and Disposal Liabilities | - | 898,719 | 898,719 |
| Federal Employment Benefits Payable | - | (73,191) | (73,191) |
| Advances from Others and Deferred Revenue | 993,880 | (947) | 992,933 |
| Other Liabilities | 4,735 | 17,008 | 21,743 |
| **Financing Sources:** | | | |
| Imputed Financing | (229,987) | - | (229,987) |
| **Total Components of Net Cost That are Not Part of Net Outlays** | **(5,147,240)** | **(29,361,707)** | **(34,508,947)** |
| **Components of Net Outlays That are Not Part of Net Cost** | | | |
| Acquisition of General Property, Plant and Equipment | - | 139,859 | 139,859 |
| Acquisition of Inventory and Related Property | 216,894 | 35,863,560 | 36,080,454 |
| **Financing Sources:** | | | |
| Transfer in/out without Reimbursements | - | - | - |
| **Total Components of Net Outlays That are Not Part of Net Cost** | **216,894** | **36,003,419** | **36,220,313** |
| **Miscellaneous Items** | | | |
| Other | 1,012 | 8,168 | 9,180 |
| **Total Other Reconciling Items** | **1,012** | **8,168** | **9,180** |
| **NET OUTLAYS** | **$ (40,224,385)** | **$ 40,351,957** | **127,572** |
| **Outlays, Net, Statements of Budgetary Resources** | | | **73,161** |
| **Reconciling Difference** | | | **$ 54,411** |

| FY 2022 | | | |
|---|---|---|---|
| | Intragovernmental | Other than Intragovernmental | Total |
| **NET COST** | **$ (31,998,444)** | **$ 32,731,774** | **$ 733,330** |
| **Components of Net Cost That are Not Part of Net Outlays** | | | |
| General Property, Plant and Equipment Depreciation | - | (61,188) | (61,188) |
| General Property, Plant and Equipment Disposal | - | (6,306) | (6,306) |
| Cost of Goods Sold | (5,562,520) | (27,845,094) | (33,407,614) |
| Net Gains/(Losses) | - | (365,702) | (365,702) |
| **Increase/(Decrease) in Assets:** | | | |
| Accounts Receivable, Net | (179,200) | (371,150) | (550,350) |
| Advances and Prepayments | - | (1,342) | (1,342) |
| **(Increase)/Decrease in Liabilities:** | | | |
| Accounts Payable | (35,001) | (430,343) | (465,344) |
| Environmental and Disposal Liabilities | - | 38,590 | 38,590 |
| Federal Employment Benefits Payable | - | 7,955 | 7,955 |
| Advances from Others and Deferred Revenue | (597,188) | 973 | (596,215) |
| Other Liabilities | 12,713 | (24,400) | (11,687) |
| **Financing Sources:** | | | |
| Imputed Financing | (165,400) | - | (165,400) |
| **Total Components of Net Cost That are Not Part of Net Outlays** | **(6,526,596)** | **(29,058,007)** | **(35,584,603)** |
| **Components of Net Outlays That are Not Part of Net Cost** | | | |
| Acquisition of General Property, Plant and Equipment | - | 125,508 | 125,508 |
| Acquisition of Inventory and Related Property | 232,853 | 35,309,865 | 35,542,718 |
| **Financing Sources:** | | | |
| Transfer in/out without Reimbursements | (479) | - | (479) |
| **Total Components of Net Outlays That are Not Part of Net Cost** | **232,374** | **35,435,373** | **35,667,747** |
| **Miscellaneous Items** | | | |
| Other | 530 | (5,232) | (4,702) |
| **Total Other Reconciling Items** | **530** | **(5,232)** | **(4,702)** |
| **NET OUTLAYS** | **$ (38,292,136)** | **$ 39,103,908** | **811,772** |
| **Outlays, Net, Statements of Budgetary Resources** | | | **770,937** |
| **Reconciling Difference** | | | **$ 40,835** |

The Net Cost to Net Outlays Reconciliation schedule reconciles the Net Cost (reported in the Statements of Net Cost) to the Net Outlays (reported in the Combined Statements of Budgetary Resources). The reconciliation clarifies the relationship between budgetary and proprietary accounting information. Examples of the reconciling items identified are: 1) Transactions which did not result in an outlay but did result in a cost; and 2) Unpaid expenses included in the net cost in this reporting period but not yet included in outlays. Components of net cost that are not part of net outlays are most commonly (1) the result of allocating assets to expenses over more than one reporting period (e.g., depreciation) and the write-down of assets (due to revaluations); (2) the temporary timing differences between outlays/receipts and the operating expense/revenue during the period; and (3) cost financed by other Federal entities (imputed inter-entity cost).

For FY 2023, the key reconciling differences between the net cost and the net outlays for DLA WCF included: (1) the Cost of Goods Sold were operating expenses for inventory purchases and have no impact on net outlays; (2) Accounts Payable for goods and services received but not yet paid for and have no impact on net outlays; (3) future funded expenses related to Environmental and Disposal Liabilities that have no impact on net outlays; (4) Advances from Others and Deferred Revenue due to additional cash advances from the HHS related to COVID-19 relief efforts (refer to Note 16, *COVID-19 Activity*); and (5) the acquisition of capital assets that have no impact on net cost.

For FY 2022, the key reconciling differences between the net cost and the net outlays for DLA WCF included: (1) the Cost of Goods Sold were operating expenses for inventory purchases and have no impact on net outlays; (2) Advances from Others and Deferred Revenue were primarily due to additional cash advances from the HHS related to COVID-19 relief efforts (refer to Note 16, *COVID-19 Activity*); and (3) the acquisition of inventory were capitalized expenditures paid for, and have no impact on net cost.

The resulting reconciling difference is primarily due to limitations of financial and nonfinancial management processes and systems that support the financial statements, as disclosed in Note 1.B., *Basis of Presentation and Accounting*.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Revenue, and Gains, Inventory and Related Property, Net, Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions, Accounts Payable, Undelivered Orders, and Reconciliation of Net Cost to Net Outlays.)

**Boom Guide**

Marine Corps Sgt. Alejandro Jaramillomora guides an all-terrain crane boom during a simulated aircraft recovery as part of Exercise Active Shield 22 at Marine Corps Air Station Iwakuni, Japan, Nov. 15, 2022. Exercise Active Shield is conducted annually with the Japan Self-Defense Force to better prepare the air station's incident response. **Photo by:** Marine Corps Cpl. Alexander Lesko


**Next Generation Pharmaceutical Contract Provides Major Benefits**

U.S. Navy Hospital Corpsman 3rd Class Michael Rodriguez, assigned to the aircraft carrier USS John C. Stennis (CVN 74), organizes pharmacy medication on the floating accommodation facility, in Newport News, Virginia, May 17, 2022. A DLA Troop Support Medical team awarded a next generation pharmaceuticals prime vendor contract, on July 14, that will provide additional benefits to military customers and their dependents. **Photo by:** Mass Communication Specialist 3rd Class Jesus Aguiar

# Note 16: COVID-19 Activity (Unaudited)

HHS entered into Intragovernmental Agency Agreements (IAAs) with DLA for DLA SCM to deliver goods and services. These goods include ventilators, Battelle sterilization units, personal protective equipment, medical supplies, food supplies and test kits to support the National COVID-19 response through the Public Health and Social Services Emergency Fund (Provider Relief Fund) appropriated as part of the Coronavirus Aid, Relief, and Economic Security Act.

DLA WCF has received a total of $894.3 million and $3.2 billion in cash advances to support COVID-19 requirements from HHS for the years September 30, 2023 and 2022, respectively. In addition, DLA has reimbursable agreements without advances with HHS totaling $990.3 million and $194.0 million for the years ended September 30, 2023 and 2022, respectively. HHS has remaining funding of $623.6 million and $1.3 billion for the years ended September 30, 2023 and 2022, respectively.

COVID-19 activities for DLA SCM are summarized by supply chain and scope for the years ended September 30, 2023 and 2022 (dollars in thousands):

Continued on next page ▶

| HHS FY 2023 | | | | | |
|---|---|---|---|---|---|
| DLA Organization | Item Description | Unfilled Customer Orders with Advance | Unfilled Customer Orders without Advance | Earned Revenue | Available Reimbursable Amount |
| Medical | Ventilators Test Components & Kits | $ 885,304 | $ 853,452 | $ 1,251,097 | $ 487,659 |
| C&E and Medical | PPE | - | 532 | - | 532 |
| C&E | PPE and Battelle CCDS Systems | - | 112,227 | 1,109 | 111,118 |
| C&E and C&T | PPE for Surge Sites | 9,050 | 53 | 8,925 | 178 |
| C&T | PPE | - | 24,061 | - | 24,061 |
| C&T and Medical | PPE | - | (12) | (15) | 3 |
| **Total** | | **$ 894,345** | **$ 990,313** | **$ 1,261,116** | **$ 623,551** |

| HHS FY 2022 | | | | | |
|---|---|---|---|---|---|
| DLA Organization | Item Description | Unfilled Customer Orders with Advance | Unfilled Customer Orders without Advance | Earned Revenue | Available Reimbursable Amount |
| Medical | Ventilators Test Components & Kits | $ 3,144,809 | $ 52,502 | $ 2,006,556 | $ 1,190,755 |
| C&E and Medical | PPE | - | 532 | - | 532 |
| C&E | PPE and Battelle CCDS Systems | - | 119,140 | 6,913 | 112,227 |
| C&E and C&T | PPE for Surge Sites | 40,810 | 47 | 31,753 | 9,104 |
| C&T | PPE | - | 20,553 | (3,508) | 24,061 |
| C&T and Medical | PPE | - | 1,246 | 1,258 | (12) |
| **Total** | | **$ 3,185,619** | **$ 194,020** | **$ 2,042,972** | **$ 1,336,667** |

### LA Distribution hosts the DDXX Academy

DLA Distribution Expeditionary reservists and civilians pose for a photo during the DLA Distribution Expeditionary Academy on April 21, at DLA Distribution San Joaquin. **Photo By:** Julian Temblador

The DLA WCF recognized revenue in relation to the COVID-19 relief effort totaling $1.3 billion for the year ended September 30, 2023, which consists of revenue recognized from HHS above totaling $1.3 billion for DLA WCF Troop Support.

The impact of COVID-19 activity to Fund Balance with Treasury (refer to the Balance Sheets and Note 3, *Fund Balance with Treasury*), Accounts Receivable (refer to the Balance Sheets and Note 4, *Accounts Receivable, Net*), Accounts Payable (refer to the Balance Sheets), Net Position (refer to the Balance Sheets and Statements of Changes in Net Position), Gross Cost (refer to the Statements of Net Cost), and New Obligations (refer to the Combined Statements of Budgetary Resources) cannot be quantified due to limitations of financial and nonfinancial management processes and systems that support the financial statements, as disclosed in Note 1.B., Basis of Presentation and Accounting, and the MD&A Analysis of Systems, Controls and Legal Compliance: Compliance with Laws and Regulations, DATA Act.

**Paint Project**

Marines paint a wall at the Tiniguiban Barangay Child Development Center during Kamandag 6, a bilateral exercise, in Palawan, Philippines, Oct. 11, 2022. **Photo by:** Marine Corps Sgt. Dana Beesley


### Fast Rope and Extraction

Soldiers assigned to the 1st Battalion, 502nd Infantry Regiment, 2nd Brigade Combat Team, 101st Airborne Division and 3rd Battalion, 501st Aviation Regiment, Combat Aviation Brigade, 1st Armored Division conduct fast rope insertion and extraction training at Mihail Kogălniceanu Airbase in Romania, Nov. 10, 2022. Soldiers continue to reinforce NATO's eastern flank and reaffirm the commitment to the European continent. **Photo by:** Army Sgt. Khalan Moore

# Required Supplementary Information (Unaudited)

## Deferred Maintenance and Repairs

The DLA WCF pays for the operating cost of five stewardship properties. These properties were transferred in FY 2020 to the Department of the Army, and the Army is responsible for all financial reporting for these assets (i.e., financial reporting and disclosures such as, but not limited to, note disclosures, deferred maintenance and repair, and other required supplemental information (RSI)). DLA WCF and the Army continue to negotiate the final transfer of all responsibilities of these assets as of September 30, 2023. In addition, DLA also pays for operation costs related to RP transferred out to other Military Services since FY 2020 and continue usage of these properties.

Therefore, DLA WCF included the additional disclosure related to the maintenance and repair needs of these assets, which were identified primarily through the condition assessment process. Maintenance and repairs that were not performed when they should have been or were scheduled and delayed for a future period are considered Deferred Maintenance and Repairs (DM&R). DM&R for the years ended September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2022 | FY 2023 |
|---|---|---|
| Active | | |
| Category 1: Building, Structures, and Linear Structure (Enduring Facilities) | $ 1,254,632 | $ 1,373,767 |
| Category 2: Building, Structures, and Linear Structure (Heritage Assets) | 15 | 1,100 |
| Total Active | $ 1,254,647 | $ 1,374,867 |
| | | |
| Inactive and Excess | | |
| Category 3: Building, Structures, and Linear Structure (Excess Facility or Planned for Replacement) | $ - | $ - |
| Total Inactive and Excess | | |
| **Total Deferred Maintenance** | **$ 1,254,647** | **$ 1,374,867** |

**M&R Policies** Installation & Equipment (DM-I) manages only the DLA Non-Energy portion of the Sustainment, Restoration, and Maintenance (SRM) program. DLA Energy runs a separate SRM program independent of DM-I. DM-I continues to conduct condition assessments of DLA Non-Energy facilities using the USACE Sustainment Management System (SMS) BUILDER. The Under Secretary of Defense memorandum dated September 10, 2013, mandated use of the reported SMS BUILDER for all DoD facilities. BUILDER captures all assessed facility deficiencies or work items categorized by fiscal year along with a cost estimate. As a result, BUILDER generates a consistent and uniform Facility Condition Index (FCI) for assessed DoD facilities.

**M&R Prioritization** Planning, programming, and execution of the DLA Non-Energy SRM program is executed IAW DLAI 4165.02 (dated 16 Feb 2022) using the following priorities:

a. Life, health, and safety concerns (cannot mitigate)
b. Facilities with an FCI of 60 or less
c. Security deficiencies including cyber security (cannot mitigate)
d. Environmental deficiencies addressing non-compliance (cannot mitigate)

e. Warfighter support facilities (mission failure)
f. Energy conservation projects (as mandated)
g. Warfighter support facilities (mission impact)
h. Routine maintenance (no mission impact)

Field sites submit their candidate projects ranked with the above-prioritized criteria. Prioritized DLA Non-Energy projects, forming a 1 – N list, are submitted to a Sustainment (maintenance and repair) board for review and voting similar to the MILCON Installation Level Review Board. The DLA Chief of Staff and DLA's MSCs chiefs of staff chair the Sustainment board. Approved projects above the MSC funding line move forward for execution based on the priority list.

For DLA Energy, the SRM program is executed in accordance with DLA Energy P-12 and the DLA Energy SRM Handbook. All work is prioritized by the Service Control Point in accordance with Service and DoD mission priorities.

**Acceptable Condition Standards** OSD and DLA considers an asset acceptable when it is in good condition with an assigned minimum FCI of 80%. Failing facilities have an FCI below 60% whereas facilities are classified in "Poor" condition with an FCI between 60 and 79. This acceptance criterion is in accordance with the Under Secretary of Defense memorandum dated April 29, 2014, titled Facility Sustainment and Recapitalization Policy. DLA also considers life, health, safety, and mission when assessing acceptable conditions. For Non-Energy, BUILDER has three separate criteria to assist in the assessment of DLA facilities: the FCI, Condition Index (CI), and BUILDER Condition Index (BCI). Those technical criteria are used differently to assess facility conditions.

**Capitalization of DM&R** The deferred maintenance and repair information presented relates to all DLA operated DoD facilities where DLA has the maintenance responsibility and is not solely restricted to capitalized assets.

**Asset Exclusions** The deferred maintenance and repair information include only facilities in Active and To Be Acquired status. It excludes facilities in a semi-active status, caretaker, out granted, non-functional, environmental hold status, closed, disposed, excess, surplus, or returned to the service Components.

**Changes Year-to-Year** The change of deferred maintenance and repair balance is due in large part to cost increases over the Congressional Notification (CN) threshold in late September. This did not leave enough time to have the CN completed before the end of FY 2023. DLA anticipates these projects will be funded in FY 2024. The decrease in the DLA Plant Replacement Value (PRV) is due to changes in asset valuation in EBS, as well as reduction in DLA footprint due to removal of obsolete real property records and the demolition of facilities. For the SRM Non-Energy BUILDER, deferred maintenance and repair data accounts for the official inflation factor of 2.1% from year to year. That inflation factor will be adjusted in BUILDER in FY 2024 and is currently under review.

For Heritage facilities (Non-Energy), the PRV increased slightly due to asset valuation; however, the deferred maintenance and repair balance of these facilities increased significantly. Reasons for the increase in Heritage facility percentage include updated condition assessments, as well as SRM projects not being executed for these low priority facilities.

With continued improvements in the SMS BUILDER Database reporting and an increased SRM budget to address facilities deficiencies and the backlog of deferred maintenance and repairs, the DLA BUILDER Portfolio will continue to show significant progress to meeting OSD mandated program objectives and goals.

# Combining Statements of Budgetary Resources

The Combining Statements of Budgetary Resources combines the availability, status, and outlays of DLA WCF's budgetary resources. The following schedules provide the Combining Statements of Budgetary Resources disaggregated by DLA WCF activities for the years ended September 30, 2023 and 2022 respectively.

(Refer to Note 1.B., *Basis of Presentation and Accounting*, related to Combined Statements of Budgetary Resources.)

## Combining Statement of Budgetary Resources

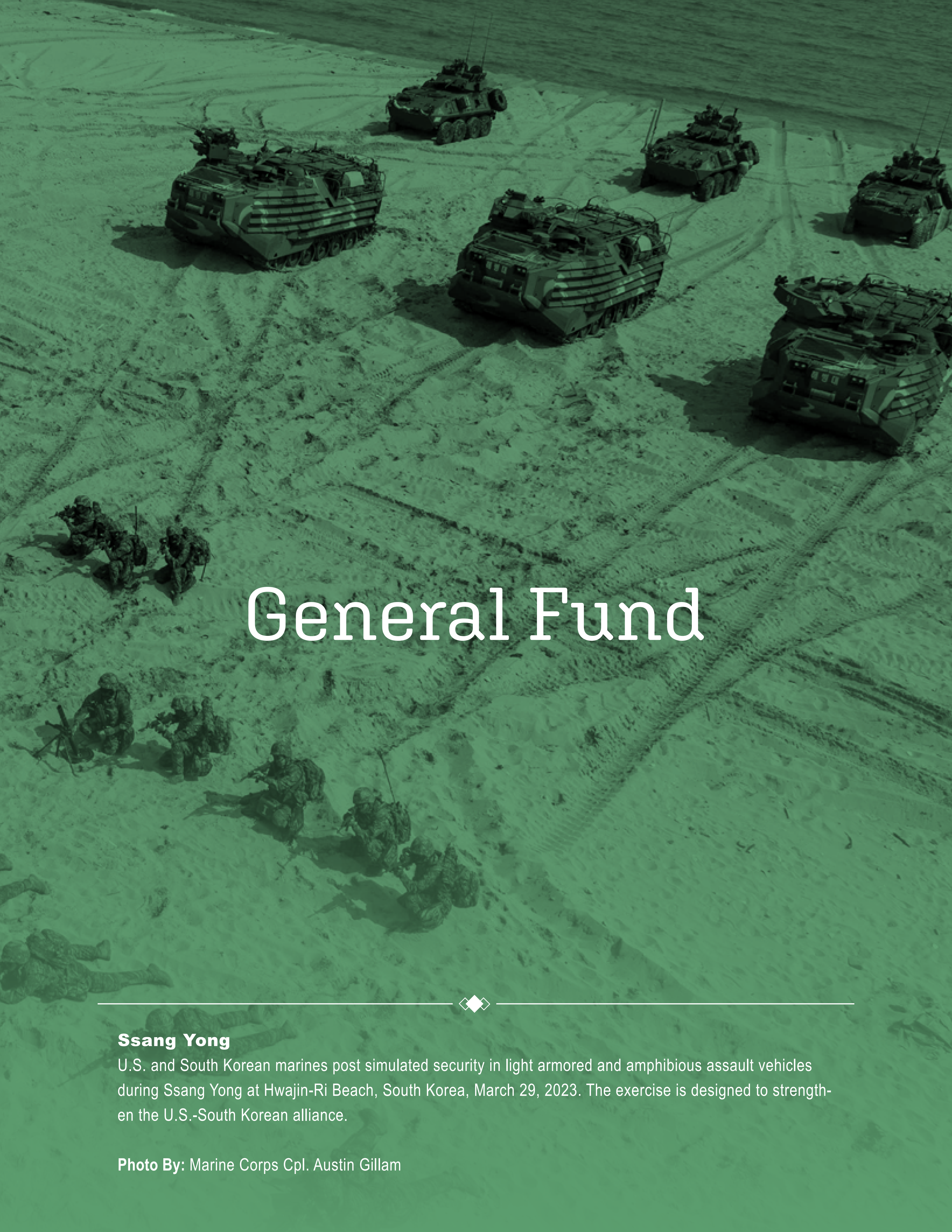
For the Year Ended September 30, 2023 (dollars in thousands)

| | Energy | Supply Chain Management | Document Services | FY 2023 Total |
|---|---|---|---|---|
| **BUDGETARY RESOURCES** | | | | |
| Unobligated Balance from Prior Year Budget Authority, Net | $ 860,447 | $ 236,018 | $ 114,657 | $ 1,211,122 |
| Appropriations | 353,114 | - | 2 | 353,116 |
| Contract Authority | 21,096,155 | 35,678,390 | 4,380 | 56,778,925 |
| Spending Authority from Offsetting Collections | - | - | 321,458 | 321,458 |
| **TOTAL BUDGETARY RESOURCES** | **$ 22,309,716** | **$ 35,914,408** | **$440,497** | **$ 58,664,621** |
| **STATUS OF BUDGETARY RESOURCES** | | | | |
| New Obligations and Upward Adjustments | $ 22,238,859 | $ 35,699,780 | $ 304,964 | $ 58,243,603 |
| Unobligated Balance, End of Year: | | | | |
| Apportioned, Unexpired Accounts | 70,857 | 214,628 | 135,533 | 421,018 |
| Unapportioned, Unexpired accounts | - | - | - | - |
| Unexpired Unobligated Balance, End of Year | 70,857 | 214,628 | 135,533 | 421,018 |
| Total Unobligated Balance, End of Year | 70,857 | 214,628 | 135,533 | 421,018 |
| **TOTAL BUDGETARY RESOURCES** | **$ 22,309,716** | **$ 35,914,408** | **$ 440,497** | **$ 58,664,621** |
| **OUTLAYS, NET** | | | | |
| Outlays, Net | $ (201,164) | $ 294,200 | $ (19,874) | $ 73,162 |
| **AGENCY OUTLAYS, NET** | **$ (201,164)** | **$ 294,200** | **$ (19,874)** | **$ 73,162** |

# Combining Statement of Budgetary Resources

For the Year Ended September 30, 2022 (dollars in thousands)

| | Energy | Supply Chain Management | Document Services | FY 2022 Total |
|---|---|---|---|---|
| **BUDGETARY RESOURCES** | | | | |
| Unobligated Balance from Prior Year Budget Authority, Net | $ 2,640,056 | $ 739,717 | $ 126,363 | $ 3,506,136 |
| Appropriations | 40,000 | 88,730 | - | 128,730 |
| Contract Authority | 19,053,389 | 33,339,667 | - | 52,393,056 |
| Spending Authority from Offsetting Collections | 1 | 474 | 268,878 | 269,353 |
| **TOTAL BUDGETARY RESOURCES** | **$ 21,733,446** | **$ 34,168,588** | **$ 395,241** | **$ 56,297,275** |
| **STATUS OF BUDGETARY RESOURCES** | | | | |
| New Obligations and Upward Adjustments | $ 20,992,519 | $ 33,932,832 | $ 290,815 | $ 55,216,166 |
| Unobligated Balance, End of Year: | | | | |
| Apportioned, Unexpired Accounts | 740,927 | 235,756 | 104,426 | 1,081,109 |
| Unexpired Unobligated Balance, End of Year | 740,927 | 235,756 | 104,426 | 1,081,109 |
| Total Unobligated Balance, End of Year | 740,927 | 235,756 | 104,426 | 1,081,109 |
| **TOTAL BUDGETARY RESOURCES** | **$ 21,733,446** | **$ 34,168,588** | **$ 395,241** | **$ 56,297,275** |
| **OUTLAYS, NET** | | | | |
| Outlays, Net | $ 2,312,942 | $ (1,549,452) | $ 7,447 | $ 770,937 |
| **AGENCY OUTLAYS, NET** | **$ 2,312,942** | **$ (1,549,452)** | **$ 7,447** | **$ 770,937** |



# General Fund

**Ssang Yong**

U.S. and South Korean marines post simulated security in light armored and amphibious assault vehicles during Ssang Yong at Hwajin-Ri Beach, South Korea, March 29, 2023. The exercise is designed to strengthen the U.S.-South Korean alliance.

**Photo By:** Marine Corps Cpl. Austin Gillam

# Audit Reports

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

November 8, 2023

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)/
CHIEF FINANCIAL OFFICER, DOD
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Transmittal of the Independent Auditor's Reports on the Defense Logistics Agency General Fund Financial Statements and Related Notes for FY 2023 and FY 2022
(Project No. D2023-D000FE-0047.000, Report No. DODIG-2024-019)

We contracted with the independent public accounting firm of Ernst & Young, LLP (EY) to audit the Defense Logistics Agency (DLA) General Fund Financial Statements and related notes as of and for the fiscal years ended September 30, 2023, and 2022. The contract required EY to provide a report on internal control over financial reporting and compliance with provisions of applicable laws and regulations, contracts, and grant agreements, and to report on whether the DLA's financial management systems substantially complied with the requirements of the Federal Financial Management Improvement Act of 1996. The contract required EY to conduct the audit in accordance with generally accepted government auditing standards (GAGAS); Office of Management and Budget audit guidance; and the Government Accountability Office/Council of the Inspectors General on Integrity and Efficiency, "Financial Audit Manual," Volume 1, May 2023, Volume 2, May 2023, and Volume 3, June 2023. EY's Independent Auditor's Reports are attached.

EY's audit resulted in a disclaimer of opinion. EY could not obtain sufficient, appropriate audit evidence to support the reported amounts within the DLA General Fund Financial Statements. As a result, EY could not conclude whether the financial statements and related notes were presented fairly and in accordance with Generally Accepted Accounting Principles. Accordingly, EY did not express an opinion on the DLA General Fund FY 2023 and FY 2022 Financial Statements and related notes.

EY's separate report, "Report of Independent Auditors on Internal Control Over Financial Reporting," discusses eight material weaknesses related to the DLA's internal controls over financial reporting.* Specifically, EY's report stated that the DLA did not:

- value and reconcile Property, Plant, and Equipment;
- reconcile Fund Balance with Treasury;
- record Accounts Receivable and revenue transactions properly;
- support Accounts Payable, expenses, and related budgetary balances;
- design controls over the financial statement reporting process to identify and prevent inaccurate balances and footnotes;
- document end-to-end business processes, monitor internal control risks, and remediate audit findings;
- record progress payments on long-term production contracts; or
- ensure the effective design and operation of financial reporting information systems.

EY's additional report, "Report of Independent Auditors on Compliance and Other Matters," discusses two instances of noncompliance with provisions of applicable laws and regulations, contracts, and grant agreements. Specifically, EY's report describes instances in which the DLA's financial management systems did not comply with the Federal Financial Management Improvement Act of 1996 and the Federal Managers' Financial Integrity Act of 1982.

In connection with the contract, we reviewed EY's reports and related documentation and discussed them with EY's representatives. Our review, as differentiated from an audit of the financial statements and related notes in accordance with GAGAS, was not intended to enable us to express, and we do not express, an opinion on the DLA General Fund FY 2023 and FY 2022 Financial Statements and related notes. Furthermore, we do not express conclusions on the effectiveness of internal controls over financial reporting, on whether the DLA's financial systems substantially complied with Federal Financial Management Improvement Act of 1996 requirements, or on compliance with

* A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting that results in a reasonable possibility that management will not prevent, or detect and correct, a material misstatement in the financial statements in a timely manner.

provisions of applicable laws and regulations, contracts, and grant agreements. Our review disclosed no instances where EY did not comply, in all material respects, with GAGAS. EY is responsible for the attached November 8, 2023 reports and the conclusions expressed within the reports.

We appreciate the cooperation and assistance received during the audit. If you have any questions, please contact me.

FOR THE INSPECTOR GENERAL:

Lorin T. Venable

Lorin T. Venable, CPA
Assistant Inspector General for Audit
Financial Management and Reporting

Attachments:
As stated

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# Report of Independent Auditors

The Director of the Defense Logistics Agency and the
Inspector General of the Department of Defense

## Report on the Audit of the Financial Statements

### *Disclaimer of Opinion*

We were engaged to audit the financial statements of the General Fund (GF) of the Defense Logistics Agency (DLA), which comprise the balance sheets as of September 30, 2023 and 2022, and the related statements of net cost and changes in net position and combined statements of budgetary resources for the years then ended, and the related notes (collectively referred to as the "financial statements").

We do not express an opinion on the accompanying financial statements of DLA. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

### *Basis for Disclaimer of Opinion*

DLA continues to have unresolved accounting issues and material weaknesses in internal controls that cause DLA to be unable to provide sufficient evidential support for complete and accurate financial statements on a timely basis. As a result of these matters, we were unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded balances and the elements making up DLA's financial statements as of and for the years ended September 30, 2023 and 2022.

### *Departures from U.S. Generally Accepted Accounting Principles*

As described in Note 1, DLA has not implemented certain accounting standards for the Department of Defense and the federal government. The effect of these matters on DLA's financial statements as of and for the years ended September 30, 2023 and 2022 is not currently determinable by DLA and could be material.

### *Responsibilities of Management for the Financial Statements*

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and

fair presentation of the financial statements that are free of material misstatement, whether due to fraud or error.

***Auditor's Responsibilities for the Audit of the Financial Statements***

Our responsibility is to conduct an audit of DLA's financial statements in accordance with auditing standards generally accepted in the United States of America, in accordance with the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States (*Government Auditing Standards*), and in accordance with the provisions of Office of Management and Budget Bulletin No. 24-01, *Audit Requirements for Federal Financial Statements*, and to issue an auditor's report. However, because of the matters described in the Basis for Disclaimer of Opinion section of our report, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

We are required to be independent of DLA and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audit.

***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Required Supplementary Information, as listed in the Table of Contents, be presented to supplement the financial statements. Such information is the responsibility of management and, although not a part of the financial statements, is required by the Federal Accounting Standards Advisory Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We were unable to apply certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report. We do not express an opinion or provide any assurance on the information.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we also have issued our reports dated November 8, 2023, on our consideration of DLA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of those reports is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of DLA's internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DLA's internal control over financial reporting and compliance.

Ernst & Young LLP

November 8, 2023

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# Report of Independent Auditors on Internal Control Over Financial Reporting Based on an Engagement to Audit the Financial Statements Performed in Accordance with *Government Auditing Standards*

The Director of the Defense Logistics Agency and the
Inspector General of the Department of Defense

We were engaged to audit, in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States (*Government Auditing Standards)* and the provisions of Office of Management and Budget (OMB) Bulletin No. 24-01, *Audit Requirements for Federal Financial Statements*, the financial statements of the General Fund of the Defense Logistics Agency (DLA), which comprise the balance sheet as of September 30, 2023, and the related statements of net cost, and changes in net position and combined statement of budgetary resources for the year then ended, and the related notes (collectively referred to as the "financial statements"), and have issued our report thereon dated November 8, 2023. Our report disclaims an opinion on the financial statements because DLA continues to have unresolved accounting issues and material weaknesses in internal controls that cause DLA to be unable to provide sufficient evidential support for complete and accurate financial statements on a timely basis.

**Report on Internal Control Over Financial Reporting**

In connection with our engagement to audit the financial statements, we considered DLA's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of DLA's internal control. Accordingly, we do not express an opinion on the effectiveness of DLA's internal control. We did not consider all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA), such as those controls relevant to preparing performance information ensuring efficient operations.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as described below and in more detail in Appendix A, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described below and in Appendix A as items I through VII to be material weaknesses.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described below and in Appendix B as items I and II to be significant deficiencies.

**Material Weaknesses**

We identified the following matters involving internal control over financial reporting and its operation that we consider to be material weaknesses, as defined above:

I. Property, Plant and Equipment (PP&E) – PP&E includes internal use software (IUS) and construction-in-progress (CIP). DLA did not have policies, procedures and controls to identify and support the costs associated with the construction and completion of assets in order to properly value the assets and had weaknesses in the processes of maintaining and reconciling PP&E records. In addition, DLA did not have sufficient policies to account for leasing arrangements and whether the leasing arrangements should be accounted for as a capital or an operating lease. Therefore, DLA was unable to support the existence, completeness, rights and valuation of its PP&E. The combination of deficiencies in aggregate results in a material weakness in internal control related to PP&E. The matters identified related to PP&E are further described in Appendix A.

II. Fund Balance with Treasury (FBwT) – FBwT represents the aggregate amount of funds in DLA's account with U.S. Treasury. DLA was unable to reconcile the FBwT ending balances from the general ledger directly to U.S. Treasury. Furthermore, DLA was unable to provide detailed listings of collections and disbursements that reconcile to the general ledger. DLA, in conjunction with Defense Finance and Accounting Services (DFAS), has implemented the Cash Management Reconciliation (CMR) and Department 97 Reconciliation and Reporting Tool (DRRT) processes as mechanisms to reconcile DLA's general ledger to U.S. Treasury. However, these tools have known control deficiencies and reconciling issues. In addition, DLA did not have sufficient policies, procedures and internal controls in place for the end-to-end FBwT process. The combination of these deficiencies in aggregate results in a material weakness in internal control related to FBwT. The matters identified related to FBwT are further described in Appendix A.

III. Accounts Receivable (AR) and Revenue – AR consists of amounts owed to DLA primarily related to providing services to other federal agencies. Revenue is earned when DLA provides services to the public or other federal entities. DLA was unable to support the balances recorded as AR; properly identify valid unfilled customer orders; and had not supported transactions recorded. In addition, DLA did not have adequate policies, procedures and controls to record AR and revenue transactions in the proper period and accurately in accordance with U.S. generally accepted accounting principles (GAAP). The combination of these deficiencies in aggregate results in a material weakness in internal control related to AR and revenue. The matters identified related to AR and revenue are further described in Appendix A.

IV. Accounts Payable (AP) and Expense – AP represents the amount owed to third parties by DLA for goods and services received. Expenses are incurred and recognized when DLA receives goods and services from the public or other federal entities. DLA was unable to support the AP balance, expenses and related budgetary balances. In addition, DLA did not have adequate policies, procedures and internal controls for the procure to pay process, including the process to create and approve obligations and the process to review, record and pay invoices. Furthermore, DLA lacked adequate procedures to record obligations and accrue for liabilities incurred but not paid; to review and close invalid obligations; and DLA recorded transactions in the procure to pay process in incorrect periods. The combination of these deficiencies in aggregate results in a material weakness in internal control related to AP and expense. The matters identified related to AP and expense are further described in Appendix A.

V. Financial Reporting – Financial reporting encompasses all aspects of operations affecting DLA's ability to produce reliable financial statements and disclosures in accordance with U.S. GAAP. DLA's financial statement preparation process lacked sufficient controls to review and identify inaccurate balances within the financial statements and incomplete and inaccurate footnote disclosures. In addition, DLA lacked policies and procedures to validate account balances and monitor reporting variances between source systems, resulting in DLA recording unsupported journal vouchers (JVs) to correct the variances. Furthermore, DLA was unable to provide detailed listings for budgetary accounts that reconcile to the general ledger. The combination of these deficiencies in aggregate results in a material weakness in internal control related to financial reporting. The matters identified related to financial reporting are further described in Appendix A.

VI. Oversight and Monitoring – Oversight and monitoring relate to DLA's lack of establishment and implementation of a sufficient enterprise-wide control environment as required by OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management Internal Control*. DLA did not have an effective OMB Circular A-123 program, which impacted DLA's ability to appropriately identify and address significant risks for all key business processes. DLA did not implement appropriate internal controls, including the documentation of policies and procedures that describe DLA's environment related to end-to-end business processes, monitoring of service providers, sub allottees, related parties, systems, risks, controls and remediation of audit findings. In addition, DLA did not perform

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proper review of data/reports used in the execution of key controls. The combination of these deficiencies in aggregate results in a material weakness in internal control related to oversight and monitoring. The matters identified related to oversight and monitoring are further described in Appendix A.

VII. Accounting for Long-Term Production Contracts – A long-term production contract is an agreement between two or more parties to produce goods, which is expected to be performed over a period of more than 12 months. The progress payment clause of the Federal Acquisition Regulation (FAR) allows the government to make payments to the contractor as work is performed. DLA did not have adequate policies, procedures and controls to record progress payments in accordance with U.S. GAAP. The matters identified related to accounting for long-term production contracts result in a material weakness and are further described in Appendix A.

VIII. Information Systems – Our assessment of DLA's information technology (IT) controls and the computing environment identified deficiencies which, collectively, constitute a material weakness in the design and operation of information systems controls over financial data. Based on our review, we identified five areas of deficiency, which, when aggregated, result in a material weakness. The deficiencies relate to the following five areas:

- Access Controls
- Configuration Management
- Segregation of Duties Controls
- Security Management/Governance Over Implementation of Security Controls
- IT Operations

The matters identified related to information systems are further described in Appendix A.

**Significant Deficiencies**

We identified the following matters involving internal control over financial reporting and its operation that we consider to be significant deficiencies, as defined above:

I. Environmental Liabilities (EL) – ELs are comprised of cleanup costs associated with the restoration of sites on real property that DLA manages. DLA lacked adequate controls to evaluate the completeness and measurement of the ELs and the ELs recorded in the financial statements. The matters identified related to EL are further described in Appendix B.

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***DLA's Response to Findings***

*Government Auditing Standards* require the auditor to perform limited procedures on DLA's response to the findings identified in our engagement to audit and described in the accompanying Management's Response to Audit Reports dated November 8, 2023. DLA's response was not subjected to the other auditing procedures applied in the engagement to audit the financial statements, and, accordingly, we express no opinion on the response.

***Purpose of This Report***

The purpose of this report is solely to describe the scope of our testing of internal control and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control. This report is an integral part of an engagement to perform an audit in accordance with *Government Auditing Standards* in considering the entity's internal control. Accordingly, this communication is not suitable for any other purpose.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2023 on our tests of DLA's compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DLA's compliance.

Ernst + Young LLP

November 8, 2023

## Appendix A – Material Weaknesses

### I. Property, Plant and Equipment

Property, Plant and Equipment (PP&E) is comprised of internal use software (IUS) and construction-in-progress (CIP). In accordance with FMFIA, management is responsible for establishing and maintaining effective controls to achieve proper accountability for property and other assets for which the agency is responsible. However, DLA was not able to support the existence, completeness, rights and obligations, or valuation of its PP&E.

A. **Lack of or Inadequate Documentation of Accounting Policies and Procedures, Including Controls.** PP&E process documentation, policy memoranda and standard operating procedures failed to document the end-to-end processing of PP&E transactions and related internal control activities. Specifically, a complete inventory and reconciliation of CIP had not been performed. DLA is in the process of establishing or revising its policies and procedures for performing the inventories and reconciliations on an ongoing basis and transferring of CIP assets upon completion.

B. **Lack of or Inadequate Documentation to Substantiate PP&E and PP&E-Related Transactions.** DLA was unable to provide documentation that PP&E balances exist and are complete, that transactions occurred or that DLA has rights to the PP&E recorded in the financial statements. Specifically, documentation was not available to support the existence and completeness of CIP assets.

C. **Lack of or Inadequate Policies, Procedures and Controls Over PP&E Processes.** DLA lacked or did not have adequate policies, procedures and controls, including the design of controls over the following:
   - **Inadequately Designed Controls Over PP&E Processes.** Controls that have been implemented were not designed adequately. For example, the information used in the control activity is not assessed for completeness and accuracy. In addition, sufficient documentation did not exist to evidence the performance of the control activities. As a result, DLA was unable to demonstrate that control activities were operating effectively.
   - **CIP.** Controls that have been designed to reconcile transactional data from construction agents to CIP balances on the financial statements were not executed.
   - **IUS.** DLA policy states that IUS assets are recorded as in-service PP&E upon the completion of the asset. However, IUS activity was not evaluated to determine whether the activity should be capitalized or expensed and to identify when assets are completed and should be placed in service.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** DLA did not have policies, procedures and controls to effectively implement accounting standards, causing inaccurate presentation of PP&E on the balance sheet and in the related footnote disclosure. Specifically, DLA neither implemented nor applied the accounting and valuation methodologies set forth by Statement of Federal Financial Accounting Standards (SFFAS) No. 5, *Accounting for Liabilities of the Government*; SFFAS No. 6, *Accounting for Property, Plant and Equipment*; SFFAS No. 10, *Accounting for Internal Use Software*; and SFFAS No. 50, *Establishing Opening Balances for Property, Plant and Equipment.* For example:

- DLA was unable to support the values assigned to IUS in accordance with SFFAS No.10.
- DLA had not established a policy to account for its leasing arrangements, nor assessed whether the leasing arrangements should be accounted for as a capital or an operating lease. As a result, the financial statements did not include disclosures for DLA's policy to account for lease arrangements, any operating lease commitments and future minimum payments due.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Lack of or Inadequate Documentation of Accounting Policies and Procedures, Including Controls.** Document, update and finalize the process cycle memoranda (PCM) that document the end-to-end processes and controls for PP&E, including monitoring and reconciling funding provided to construction agents and the transfer of CIP assets to the military services when they are placed into service. Complete the inventory of CIP to verify the existence and completeness of the accounting records.

B. **Lack of or Inadequate Documentation to Substantiate PP&E and PP&E-related Transactions.** Develop documentation to substantiate that all of DLA's CIP assets exist and are recorded completely and accurately.

C. **Lack of or Inadequate Policies, Procedures and Controls Over PP&E Processes.**
   - **Inadequately Designed Controls Over PP&E Processes.** Design and implement internal control activities that include criteria, analyses, reviews and supporting thresholds used in the execution of all relevant internal controls. Specifically, evidential matter should be available to demonstrate that the control activity was performed; the scope of the review should be sufficient to identify and correct errors in the procedures performed; and the assessment of any variances should be performed appropriately.
   - **CIP.** Execute internal controls to ensure DLA has appropriate oversight, review and monitoring of CIP assets and related balances recorded on the financial statements.
   - **IUS.** Design and implement policies and procedures that require IUS activity to be reviewed for proper capitalization, recorded in the appropriate period and classified appropriately when assets are completed and placed in service.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** Design policies, procedures and control to implement the appropriate accounting standards, specifically SFFAS No. 5, SFFAS No. 6, SFFAS No. 10 and SFFAS No. 50. The policies, procedures and controls should include:
   - Assessing whether the values assigned to IUS assets are in accordance with SFFAS No. 10. In addition, evaluate alternative valuation methodologies available under SFFAS No. 50. SFFAS No. 50 permits the exclusion of IUS and IUS under development from the opening balance as of the opening balance date.
   - Establishing an accounting policy to identify and account for leasing arrangements, including whether the leases should be accounted for and reported as capital or operating leases in accordance with SFFAS No. 5 and SFFAS No. 6. In addition, include the required disclosures for capital and operating leases in the financial statements in accordance with OMB Circular A-136.

## II. Fund Balance with Treasury

Fund Balance with Treasury (FBwT) represents the aggregate amount of funds in DLA's account with U.S. Treasury. Treasury's Financial Manual (TFM) Chapter 5100, Sections 5125 and 5130 requires agencies to implement effective and efficient reconciliation processes and perform timely reconciliations. However, deficiencies existed related to DLA's processes of recording and reconciling transactions involving FBwT.

A. **Lack of or Inadequate Documentation of FBwT Accounting Policies, Procedures and Controls.** DLA did not document the end-to-end process to account for, monitor and report FBwT and FBwT-related transactions.
   - **Suspense Accounts.** The documentation did not include the process to correctly identify and resolve suspense amounts.
   - **Reconciling Items to Treasury**. The documentation did not include the processes to correct and review undistributed transactions identified in the Department 97 Report Reconciliation Tool (DRRT) report in a timely manner.

B. **Lack of Controls for the Reconciliation of FBwT Between the General Ledger and the U.S. Treasury.** DLA, in conjunction with DFAS, has implemented the CMR and DRRT processes as mechanisms to attempt to tie the general ledger to U.S. Treasury. However, the CMR and DRRT processes were not sufficient to produce a complete and accurate reconciliation of DLA's general ledger to U.S. Treasury. As a result, DLA was unable to accurately reconcile to U.S. Treasury.

C. **Lack of or Inadequate Documentation to Substantiate FBwT.** DLA was unable to provide listings of collection and disbursement transactions at the detailed voucher level that reconcile to the general ledger. As such, the FBwT transactions were not appropriately supported.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation of FBwT Accounting Policies, Procedures and Controls.** Finalize the documentation of the end-to-end process for FBwT. The documentation should include the process to perform regular and recurring reconciliations of the suspense account data and the process to research and resolve differences between U.S. Treasury, disbursing system records and accounting system records within a timely basis.

B. **Lack of Controls for the Reconciliation of FBwT Between the General Ledger and the U.S. Treasury.** In coordination with DFAS, obtain a system and organization controls (SOC) report for the CMR and DRRT and reconcile the transactions recorded in the general ledger to the transactions sent to the U.S. Treasury systems in order to verify that the data was processed correctly.

C. **Lack of or Inadequate Documentation to Substantiate FBwT.** Develop and implement procedures to generate complete and accurate listings of FBwT collections and disbursement transactions at the detailed voucher level that reconcile to the general ledger.

### III. Accounts Receivable and Revenue

Accounts receivable (AR) consists of amounts owed to DLA. Revenue is earned when DLA provides services to the public or other federal entities. Unfilled Customer Orders (UCOs) represent the amount of goods and/or services to be furnished to other federal government entities and for the public. AR, revenue and UCOs fall within the scope of DLA's order-to-cash process. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls that provide reasonable assurance that revenues and budgetary transactions applicable to the agency's operations are properly recorded and accounted for to permit the preparation of reliable financial reports and maintain accountability of assets. DLA has a significant volume of intra-governmental transactions in the order-to-cash process, which represent reimbursable agreements to provide services to its ultimate consumers. The volume of these transactions makes it critical for DLA to properly record and reconcile these transactions to ensure timely, appropriate recognition of costs to the end users. However, DLA was unable to support the existence of accounts receivable and unfilled customer orders and the occurrence of revenue and related budgetary transactions.

A. **Lack of or Inadequate Documentation of AR and Revenue Accounting Policies, Procedures and Controls.** DLA did not document the end-to-end process to account for UCOs.

- **UCOs**. The documentation did not include the process to review the validity of significantly aged UCOs in the general ledger despite being closed through other business processes and systems.

B. **Lack of or Inadequate Documentation to Substantiate UCOs, AR and Revenue Transactions.** DLA was unable to provide documentation that UCO and AR balances exist and are accurate, revenue and corresponding budgetary balances occurred and that transactions were recorded in the proper period. Specifically, documentation was not available to support:

- **UCOs.** The balance of UCO transactions is complete and accurate. As a result, five out of twelve samples tested were not appropriately supported.
- **Revenue.** Revenue transactions occurred, were matched with related expenses and were recorded accurately and in the proper period. As a result, two out of seven samples tested were not recorded in the proper period.
- **AR.** Receivable balances are valid and have not been collected (i.e., existence and completeness).

C. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** DLA did not have policies, procedures and controls to effectively implement accounting standards, causing inaccurate presentation of revenue on the statement of net cost and in the related footnote disclosure. Specifically, DLA did not assess the proper revenue recognition for services produced to order in accordance with SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting.*

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Lack of or Inadequate Documentation of Accounting Policies and Procedures, including Controls.** The documentation should include the process to review the aged UCO balances for validity.

B. **Lack of or Inadequate Documentation to Substantiate UCOs, AR and Revenue Transactions.** Develop documentation, including detailed listings of account balances, to substantiate that the balance of UCO, AR (federal and with the public), revenue and corresponding budgetary transactions are complete, accurate, and recorded and matched with related expenses in the proper period and that the balances exist or have occurred. The listing should be reconciled to the general ledger.

C. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** Design policies, procedures and control to implement the appropriate accounting standards, specifically SFFAS No. 7. The policies, procedures and controls should include assessing the method used to recognize revenue for specific services produced to order. Specifically, DLA should assess whether the percentage-of-completion method should be used, as prescribed by SFFAS No. 7.

## IV. Accounts Payable and Expenses

Accounts payable (AP) consists of amounts owed to vendors. Expenses are incurred and recognized when DLA obtains goods and services from the public or other federal entities. Undelivered Orders (UDOs) represent the amount of goods and/or services ordered which have not been received. AP, expenses and UDOs fall within the scope of DLA's procure-to-pay process. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls that provide reasonable assurance that expenses and budgetary transactions applicable to the agency's operations are properly recorded and accounted for to permit the preparation of reliable financial reports. Because of the nature of the operations, DLA has a significant volume of transactions to procure goods and services. Deficiencies exist in DLA's processes for recording and supporting the accounts payable and accruals, expenses and related budgetary balances; recording obligations and accounts payable in the proper period; documenting policies, procedures and controls; and designing and executing controls over the processes to create and approve obligations and to review, record and pay invoices.

A. **Lack of or Inadequate Documentation of UDOs, AP, Unliquidated Obligation (ULO) and Expenses Accounting Policies, Procedures and Controls.** DLA did not document the end-to-end process to account for UDO, AP and expense transactions.
   - **UDOs.** The documentation did not include the process to review the validity of significantly aged UDOs and UDOs funded by expired and cancelling authority.
   - **AP.** The documentation did not include the process to evaluate the validity of AP, including significantly aged AP, negative payables and AP from canceled appropriations; the process to record invoices in the general ledger and submit to DFAS for payment timely; and the process to pay invoices timely or assess interest penalties for late payments in accordance with the Prompt Payment Act.
   - **ULO.** The documentation did not include the process to review the validity of significantly aged ULO.

B. **Lack of or Inadequate Controls over UDOs, AP, Expenses and Cash Disbursement Processes.** DLA lacked or did not have adequate controls, including the design of controls, over the following:
   - **UDOs.** DLA lacked controls to approve and record obligations in a timely manner; controls to record upward and downward adjustments to UDOs accurately and timely; and controls to review and close invalid UDOs in a timely manner. For example, one of our six samples

was not accurately classified, and three of our six downward adjustment samples were not recorded within the timeframes required by DLA's policies and procedures.

- **Vendor Contracts.** DLA lacked controls to execute contracts in accordance with the Federal Acquisition Regulation (FAR) and to record obligations timely for contracts, including Indefinite Quantity Contracts (IQC). For example, IQCs awarded did not have an obligation recorded at the contract award date because the IQC did not have a guaranteed minimum at the contract award date.
- **AP and Cash Disbursements.** DLA lacked controls to post goods receipts and the related AP in a timely manner; review invoices prior to payment and review payments that fail to post systematically in a timely manner.
- **Expenses Recorded in the Appropriate Period.** DLA lacked controls to record expense transactions appropriately and accurately in the period that the transactions occurred.
- **Transactions Recorded at the Detailed Level.** DLA lacked controls to comply with the Federal Financial Management Improvement Act (FFMIA), which requires transactions to be recorded at the detailed transaction level. DLA recorded transactions at a summary level for certain budgetary and proprietary accounts. As a result, each summary-level record contained multiple individual transactions. A reconciliation was not performed between detailed transactions posted to the proprietary accounts and the summarized postings to the corresponding budgetary accounts.

C. **Lack of or Inadequate Documentation to Substantiate AP and Expense Transactions.** DLA was unable to provide documentation to support the existence of accounts payable balances, or expense transactions that occurred were accurately recorded in the financial statements. Specifically, documentation was not available to support the transactions and balances for various accounts, such as accounts payable, accounts payable from canceled appropriations, negative payables, expenses, UDOs (paid and unpaid), and upward and downward adjustments to delivered and undelivered orders. For example, DLA was unable to support two of our six downward adjustment samples.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** DLA did not have policies, procedures and controls to effectively implement accounting standards. Specifically, DLA had not implemented or applied the accounting set forth by SFFAS No. 1, *Accounting for Selected Assets and Liabilities,* No. 4, *Managerial Cost Accounting Standards and Concepts* and No. 5, *Accounting for Liabilities of the Federal Government*. For example:

- DLA processes allow for payment without receipt, thus resulting in a negative payable balance. This occurs when payment is made prior to the goods receipts being posted in the general ledger, and it results in an understatement of expenses and payables and a misstatement of UDOs. The quarterly adjustment to offset the negative payable balances recorded results in an overstatement of Accounts Payable.

- Accounts payable and accrued liabilities were not recorded appropriately. For example, DLA applied the straight-line method to calculate the accrual amount but did not perform any assessment to determine whether this is an appropriate methodology. Particularly, for agreements that do not have a fixed monthly cost, the straight-line method is not appropriate.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation of UDOs, AP, ULO and Expenses Accounting Policies, Procedures and Controls.** Update and finalize the PCMs that document the end-to-end processes for UDOs, AP, ULO and expenses.
   - **UDOs.** The documentation should include the processes to review the validity of significantly aged UDOs and UDOs funded by expired and cancelling authority and include a process to write off residual UDOs for completed transactions.
   - **AP.** The documentation should include the process to evaluate the validity of accounts payable, including significantly aged AP, negative payables and AP from canceled appropriations; the process to record invoices in the general ledger and submit to DFAS for payment timely; and the process to pay invoices timely or assess interest penalties for late payment in accordance with the Prompt Payment Act.
   - **ULO.** The documentation should include the process to review the validity of significantly aged ULO, including the process to write off residual ULO for completed transactions.

B. **Lack of or Inadequate Controls over UDOs, AP, Expenses and Cash Disbursement Process**
   - **UDOs.** Design and implement controls to approve and record obligations in a timely manner; controls to record upward and downward adjustments to UDOs accurately and timely; and controls to review and close invalid UDOs in a timely manner.
   - **Vendor Contracts.** Design and implement controls to execute contracts in accordance with the FAR and record obligations timely for contracts, including IQCs. For example, controls that prevent contracts from being completed and executed without the appropriate terms and conditions required by the FAR.
   - **AP and Cash Disbursements.** Design and implement controls to post goods receipts and the related AP in a timely manner; review invoices prior to payment; and review payments, including payments that fail to post systematically, and ensure that they are posted in a timely manner.
   - **Expenses Recorded in the Appropriate Period.** Design and implement controls to record expense transactions appropriately and accurately and in the period that the transaction occurred, and controls to monitor expense transactions at or near period-end.

- **Transactions Recorded at the Detailed Level.** Design and implement controls to comply with the FFMIA and reconcile the transaction-level detail to the summarized postings in each account.

C. **Lack of or Inadequate Documentation to Substantiate AP and Expense Transactions.** Develop documentation to support that AP and corresponding budgetary balances exist, or that expense transactions occurred and are accurately recorded in the financial statements.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** Design and implement policies and procedures to record expenses incurred in the proper period and classify costs and payables in accordance with SFFAS No. 1, No. 4 and No. 5.

**V. Financial Reporting**

Financial reporting encompasses all aspects of operations affecting DLA's ability to produce reliable financial statements and disclosures in accordance with U.S. GAAP. This process starts with establishing an effective governance structure to identify and assess risk and continues with developing a control environment that is effective and efficient to manage identified risks. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls to achieve reliable financial reporting. However, deficiencies existed in DLA's processes related to the accumulation and presentation of financial position and results of operations.

A. **Lack of or Inadequate Documentation of Financial Reporting and Budgetary Policies, Procedures, and Controls.** DLA did not document the end-to-end processes related to financial reporting and funds management.

- **Financial Reporting.** The documentation did not include the processes to review and reconcile system generated reversals of prior year JVs which impact opening balances.
- **Funds Management.** The documentation did not sufficiently include a description of the process to record budget authority, the transfer process, the Treasury warrant process, or the year-end processes for cancelling and expiring funds.

B. **Lack of Controls Over Compliance with the TFM United States Standard General Ledger (USSGL).** DLA did not have controls to configure the general ledger posting logic to be compliant with the USSGL and apply TFM updates timely, nor did DLA have controls to link business events to the correct posting logic. As a result, transactions were not recorded appropriately. For example, DLA inappropriately used a general ledger account (negative payables) to track payments made without goods received and inappropriately combined entries to record the movement of budgetary funds through the apportionment and allotment process, which should be recorded separately. Additionally, DLA did not implement the TFM update to add USSGL accounts 310710 – Unexpended Appropriations – Used – Disbursed and 570010 – Expended Appropriations – Disbursed.

C. **Lack of or Inadequate Controls Over Financial Reporting Processes.** DLA lacked or did not have adequate controls, including the design of controls, over the following:

- **Beginning Balances for Budgetary Accounts.** DLA did not have controls to verify the accuracy of the beginning balances for budgetary accounts, such as Total Actual Resources Collected. As a result, DLA was unable to substantiate beginning balances recorded on the financial statements.
- **Trading Partner Transactions.** DLA did not have controls in place to validate and reconcile trading partner eliminations. Adjustments made to accounts receivable, accounts payable, revenue, expenses and undisbursed funds were not appropriately supported. A complete reconciliation was not performed at the agreement level to the trading partner adjustments that were being made. As a result, trading partner adjustments were recorded in the Defense Departmental Reporting System (DDRS) as "top-side" adjustments and were identified as "unsupported" by DFAS.
- **Contingent Liabilities.** DLA did not have adequate controls to identify and account for contingent legal liabilities that should be recorded or disclosed in the financial statements. Controls that were implemented were not adequately designed as they did not include sufficient procedures to verify the data used to assess contingent liabilities were complete and accurate.
- **Financial Statement Close Process.** DLA did not have adequately designed controls around the annual close and reconciliation processes, such as the following: the monthly or quarterly reconciliation between the unadjusted trial balance (UTB) and the adjusted trial balance (ATB), including sub allottee balances, was not performed sufficiently and timely; the information used in the reconciliation of UTB to ATB was not complete and accurate; and the review of the procedures performed during the financial statement close process was not adequate.
- **Budgetary to Proprietary Tie Points.** DLA did not have adequately designed controls around the tie-point process. There were reconciliation issues between the budgetary and proprietary tie points. As a result, DFAS recorded unsupported monthly and quarterly JV in the general ledger and DDRS to reconcile DLA's budgetary accounts to the proprietary accounts.

- **Monthly or Quarterly JV Adjustments.** DLA did not have controls to review and approve JV adjustments recorded in the general ledger and DDRS by DLA and DFAS for completeness, accuracy and validity. As a result, a comprehensive listing of adjustments made was not maintained to allow DLA to determine the appropriateness of each JV adjustment, including those recorded by their service provider.
- **Financial Statement Review Process.** The level of review of the financial statements and footnote disclosures was insufficient to detect and correct misstatements in the financial statements and related disclosures. As a result, inaccurate balances and disclosures were reported in the financial statements and notes. For example, line items were not appropriately classified between federal and with the public; supporting documentation did not support the balances recorded in the notes; and the financial statements were not prepared in conformity with U.S. GAAP as described in Note 1, Significant Accounting Policies, which did not sufficiently describe changes or noncompliance in U.S. GAAP reporting. In addition, DLA had not designed processes or controls to implement new accounting standards. As a result, DLA has not implemented accounting standards such as SFFAS No. 47 *Reporting Entity* and SFFAS No. 49 *Public-Private Partnerships: Disclosure Requirements.*
- **Transactions Recorded Using Elevated Privileges.** DLA did not have adequately designed controls to review and approve transactions recorded with elevated access privileges.
- **Receipt of Budgetary Funding.** DLA did not have adequate controls to identify variances in the reconciliation of budgetary funding, including the reconciliation to the public law.

D. **Lack of or Inadequate Documentation to Substantiate Budgetary Execution.** DLA was unable to provide detailed listings for budgetary accounts at the purchase order (PO) or sales order (SO) level that reconcile to the general ledger, such as delivered and undelivered orders and unfilled customer orders. As such, the budgetary accounts were not appropriately supported.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation of Financial Reporting and Budgetary Policies, Procedures, and Controls.**
   - **Financial Reporting.** Document the financial reporting process, to accurately reflect all aspects of the end-to-end process, including processes and controls performed to reconcile prior year activity to opening balances.

- **Funds Management.** Document the funds management process and controls to accurately reflect all aspects of the end-to-end budget to execute process, including processes and controls performed by DLA and service providers.

B. **Lack of Controls Over Compliance with the TFM USSGL.** Design and implement controls to configure posting logic to be compliant with the USSGL; apply TFM updates in a timely manner; link business events to the correct posting logic; and post transactions as intended.

C. **Lack of or Inadequate Controls Over Financial Reporting Processes.**

- **Beginning Balances for Budgetary Accounts.** Design and implement control activities to accurately state the beginning balance for carryforward budgetary accounts.
- **Trading Partner Transactions.** Design and implement controls to perform a reconciliation at the agreement level to validate trading partner eliminations, which includes identifying, researching and resolving variances between DLA general ledger data and trading partners.
- **Contingent Liabilities.** Design and implement controls to verify the completeness and accuracy around system generated reports used in the execution of controls to identify, estimate, record and disclose contingent liabilities in the financial statements.
- **Financial Statement Close Process.** Develop and implement controls around the annual close and reconciliation process, which includes a complete, accurate and timely reconciliation of the UTB to the ATB, including sub allottee balances.
- **Budgetary to Proprietary Tie Points.** Design and implement controls to reconcile budgetary to proprietary tie points and investigate variances.
- **Monthly or Quarterly JV Adjustments.** Design and implement controls to review and approve JV adjustments recorded in the general ledger and DDRS by DLA and DFAS for completeness, accuracy and validity prior to posting.
- **Financial Statement Review Process**. Design and implement controls to sufficiently review the quarterly and annual financial statements and disclosures; to detect and correct misstatements; and to review that the financial statements and disclosures are complete and prepared in accordance with U.S. GAAP; and to design processes and controls to analyze the impact of and implement new accounting standards, as appropriate.
- **Transactions Recorded Using Elevated Privileges.** Design and implement controls to review and approve transactions recorded with elevated access privileges to assess for completeness, accuracy and validity. The review and approval should be performed by authorized individuals, such as financial management.
- **Receipt of Budgetary Funding**. Design and implement controls to perform an adequate reconciliation of the amounts recorded in the general ledger to the Consolidated Appropriations Act and the final report on budget execution and budgetary resources.

D. **Lack of or Inadequate Documentation to Substantiate Budgetary Execution.** Develop and implement procedures to generate complete and accurate listings of budgetary accounts at the purchase order and sales order level that reconcile to the general ledger.

## VI. Oversight and Monitoring

Oversight and monitoring relate to DLA's lack of establishment and implementation of a sufficient enterprise-wide control environment as required by OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management Internal Control*.

A. **Lack of or Inadequate Documentation Around the OMB A-123 Program**. DLA did not document the end-to-end process to oversee and monitor the enterprise-level risks and controls, including the OMB A-123 program. Specifically, DLA had not performed and documented a sufficient risk assessment at the enterprise and business process level to assess and document reporting matters, such as the complexity of programs, accounting estimates, related-party transactions and the extent of manual processes; a complete and accurate population of its assessable units, business processes and relevant controls that are responsive to and mitigate risks, including fraud risks; and an assessment and plan for timely remediation of audit findings.

B. **Lack of or Inadequate Controls Around System-Generated Reports.** DLA lacked or did not have adequate controls to verify the accuracy and completeness of system-generated reports required in the execution of controls.

C. **Insufficient Oversight and Monitoring of Third-Party Service Providers.** Service organizations undergo examinations of internal controls over systems and processes supporting their customers. The results of these examinations are documented in System and Organization Controls 1 (SOC 1) reports and include the independent service auditor's report, the service organization's management assertions and identified Complementary User Entity Controls (CUECs) that users of the service organization (e.g., DLA and its sub allottees) should have in place to supplement the service organization's internal controls. DLA did not perform sufficient oversight and monitoring of SOC 1 reports and did not sufficiently design, implement or monitor CUECs over its service providers.

D. **Insufficient Oversight and Monitoring of Funding and Transactions Executed by Others.** Review controls were not designed effectively to monitor funding and report transactions executed by suballotees. Specifically, DLA did not perform a sufficient review of transactions that were recorded on their financial statements to prevent or detect misstatements. For example, the execution of funding awarded to grantees for the Procurement Technical Assistance Center (PTAC) program was not adequately monitored and inventory procured by Defense Microelectronic Activity (DMEA) with funding sub allotted from DLA was not properly reported.

***<u>Recommendations</u>***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation Around the OMB A-123 Program.** Document the end-to-end process to oversee and monitor the enterprise-level risks and controls, including the OMB A-123 program. Perform and document a sufficient risk assessment at the enterprise and business process level to assess and document reporting matters. Document a complete and accurate population of its assessable units and business processes. Identify and assess the risks in each business process and design and implement relevant controls that are responsive to and mitigate these risks, including fraud risks. Perform an assessment of audit findings and establish and execute the plan to remediate the audit findings timely.

B. **Lack of or Inadequate Controls Around System-Generated Reports.** Design and implement controls to verify the accuracy and completeness around system-generated reports used in the execution of controls. For example, the procedures should include footing system generated reports; performing a tie-out of system generated reports to the general ledger system; verifying that the parameters used to generate the reports or data are appropriate; selecting a sample of transactions or balances in the report; and validating that the transactions are accurate.

C. **Insufficient Oversight and Monitoring of Third-Party Service Providers.** Design and implement controls around the SOC 1 review process and validate that CUECs are properly identified, designed and operating effectively.

D. **Insufficient Oversight and Monitoring of Funding and Transactions Executed by Others.** Design and implement internal controls to review transactions executed by others, but recorded in DLA's financial statements, are complete and accurate, and are supported by appropriate documentation.

## VII. Accounting for Long-Term Production Contracts

Long-term production contracts consist of agreements between DLA and outside vendors to procure goods or services. The contract terms allow the government to make progress payments to the contractor as work is performed, specifically payments upon reaching certain milestones and prior to receiving the finished goods. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls that provide reasonable assurance that significant classes of transactions, such as long-term production contracts, are properly recorded and accounted for to permit the preparation of reliable financial statements. However, we identified the following deficiency in internal controls.

A. **Inadequate Controls Over Long-Term Production Contract.** DLA did not have adequate controls to review payments made to acquire goods under long-term production contracts and assess the underlying business events to determine the proper accounting. Further, DLA was unable to provide documentation that the business events were accounted for in accordance with U.S. GAAP. As a result, transactions were not recorded in accordance with U.S. GAAP.

***Recommendations***

A. **Inadequate Controls Over Long-Term Production Contracts.** Design and implement controls to review the payments made under long-term production contracts and assess the underlying business event to determine that the accounting for these transactions is in accordance with U.S. GAAP.

**VIII. Information Systems**

Information systems controls are a critical component of the federal government's operations to manage the integrity, confidentiality and reliability of its programs and activities and assist with reducing the risk of errors, fraud or other illegal acts. Information management security, access controls, segregation of duties, configuration management, and IT operations controls are fundamental to the integrity of financial data and can help manage risks such as unauthorized access, changes to critical data, and prevent compromised data. The nature, size, and complexity of DLA's operations require DLA to administer its programs under a decentralized business model by using numerous geographically dispersed operating locations and complex, extensive information systems.

Control deficiencies in the design and operation of financially significant information systems continue to occur in the information systems environment controls. The deficiencies relate to the following areas:

- Access controls
- Configuration management controls
- Segregation of duties controls
- Security management/governance over implementation of security controls
- IT operations controls

**Access Controls**

Access controls include those related to protecting system boundaries, user identification and authentication, authorization, protecting sensitive system resources, audit and monitoring, and physical security. When properly implemented, access controls can help ensure that critical systems assets are physically safeguarded and that logical access to sensitive computer programs and data is granted to users only when authorized and appropriate. Weaknesses in such controls can compromise the integrity of sensitive data and increase the risk that such data may be inappropriately used and disclosed.

The identified access control weaknesses in aggregate represent a significant risk to the DLA financial statements, Information Technology (IT) environment, and financial applications. Absent or ineffective preventative controls and compensating detective controls expose financial systems and financial data to inappropriate access, unauthorized inputs, and inaccurate entries, resulting in significant risk to the financial statements.

The identified access control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- For a selection of users of financially significant applications, access was not restricted to authorized users with a business need, was not reviewed and documented prior to provisioning, and was not assigned in accordance with the principle of least privilege.
- For a selection of account management controls for financially significant applications, user access and activity were not monitored and tracked for routine access recertification, revalidation of privileged access, and terminated or inactive users.
- For a selection of audit logging controls for one financially significant application, audit logs, security violations, and sensitive user activity were not tracked, monitored, resolved, or configured appropriately within systems.

**Configuration Management Controls**

Configuration management involves the identification and management of security features for all hardware and software components of an information system at a given point and systematically controls changes to that configuration during the system's life cycle. By implementing configuration management controls, DLA can ensure that only authorized applications and software programs are placed into production through establishing and maintaining baseline configurations and monitoring changes to these configurations. Weaknesses in such controls can compromise the integrity of sensitive data and increase the risk that such data may be inappropriately used and disclosed.

The identified configuration management and change control weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls expose financial systems and financial data to unexpected impact from changes, inappropriate or unauthorized changes, and application errors in production.

The identified change control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- For a selection of changes to one financially significant application, both routine and emergency changes were not reviewed, approved, and tested in a non-production environment prior to release. The impact and functionality of configuration changes were not assessed prior to implementation.
- For one financially significant application, system configurations, baseline code, and production environments were not monitored and inspected for unauthorized changes.
- For one financially significant application, users had access privileges enabling them to bypass the configuration management process and make changes directly to production.

**Segregation of Duties Controls**

An effective control environment guards against a particular user having incompatible functions within a system. Segregation of duties controls provide policies, procedures, and an organizational structure to prevent one or more individuals from controlling key aspects of computer-related operations and, thereby, conducting unauthorized actions or gaining unauthorized access to financial management information systems.

The identified segregation of duties and conflicting role weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls around segregation of duties allows users to circumvent processes and automated controls in place, obtain unnecessary or elevated access, and impact the integrity of financial data.

The identified weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- Segregation of duties within the user provisioning process were not completed consistently across financially significant applications. Conflicting roles were not inspected and rationalized prior to provisioning. Management did not periodically monitor segregation of duties conflicts that consider both IT and business process roles and activities.
- Application program management has not completely identified sensitive (financial transactions) roles in order to implement appropriate segregation of duties processes and controls.

**Security Management / Governance Over Implementation of Security Controls**

An entity-wide information security management and internal control program is the foundation of a security control structure to address security risks. The security management program should establish a framework and continuous cycle of activity for assessing risk, developing and implementing effective security procedures, and monitoring the effectiveness of these procedures. Without a well-designed program, security controls may be inadequate; responsibilities may be unclear, misunderstood, or improperly implemented; and controls may be inconsistently applied. Such conditions may lead to insufficient protection of sensitive or critical resources and disproportionately high expenditures for controls over low-risk resources.

The identified security management and governance weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls around internal controls and governance compound data integrity risk by not monitoring third parties and not remediating known gaps timely.

The identified security management control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- SOC 1 reports were not monitored and reviewed to assess CUECs, including validation of whether management's internal controls relevant to the CUECs, are designed, implemented, and operating effectively.
- Management internal control procedures did not identify financially significant risks, establish and implement controls, track known risk exposure, and remediate control gaps.

**IT Operations Controls**

Effective IT operations controls support the reliability of various aspects of operating the IT environment related to the complete and accurate processing of transactions and the protection of information used in that processing. IT operations involves computer job management tasks related to scheduling and running jobs (programs), monitoring the successful completion of those jobs, and detecting and addressing job failures timely. Relevant jobs may accept, process, and move data from one IT application to another via system interfaces for inclusion in financial reporting. IT administrators may also utilize programs or software that supports maintenance of the IT environment or data, including tasks responsible for backing up financially relevant programs and data.

The identified IT operations weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls around IT operations increases the risk that issues with programs that are not scheduled correctly or don't process to completion, may not be addressed, or may be addressed inappropriately, and hardware or software issues will result in the loss of financially relevant data or the ability to accurately process that data.

The identified IT operations control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- Contingency planning (CP) processes and controls failed in allowing management to backup system data.

***Recommendations***

Implement controls to address deficiencies in access controls, configuration management, segregation of duties, security management procedures, and IT operations to include:

**Access Controls**

- Restrict access to authorized users in accordance with the least privilege principle. Review and approve all access, including justification of business needs.
- Routinely monitor and revalidate access needs for business users, privileged users, and terminated and inactive users.
- Monitor user activity, identify and audit security violations, and assess privileged and sensitive users and transactions.

**Configuration Management Controls**

- Review, approve, and test changes prior to implementation, to include user testing and functionality assessments.
- Monitor source code, configurations, and production environments for unauthorized changes.
- Segregate conflicting roles between development and production environments.

**Segregation of Duties Controls**

- Identify, periodically review, and document sensitive and conflicting roles, enforce established segregation of duties processes, and assess conflicts during account provisioning and management. Segregate conflicting roles where possible, and if unavoidable, document business rationale and monitor user activity.

**Security Management/Governance Over Implementation of Security Controls**

- Establish a process to evaluate and incorporate service provider reports, findings, and controls into management's security documentation, governance process, and application control environment.
- Document risks and controls in place, identify gaps, and complete corrective actions to strengthen the internal control environment. Improve documentation, test and validate controls, and remediate findings.

**IT Operations Controls**

- Design and implement controls to periodically backup and monitor system data to successfully respond to incidents and prevent the permanent loss of data.

## Appendix B – Significant Deficiencies

### I. Environmental Liabilities

ELs are comprised of cleanup costs associated with the restoration of sites that DLA manages. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls to achieve reliable financial reporting. However, we identified the following deficiency in internal controls, which, when aggregated, we consider to be a significant deficiency.

A. **Inadequate Controls Over Estimation Processes.** DLA did not have effectively designed management review controls to evaluate the completeness and measurement of the EL and the EL recorded in the financial statements. There was a lack of sufficient evidence of management's review, including management's review of the completeness and accuracy of the information used in the valuation of the EL.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Inadequate Controls Over Estimation Processes.** Design and implement formalized management review controls that adequately document management's review of the EL, including establishing a thresholds for review, documentation of findings and actions taken by management.

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# Report of Independent Auditors on Compliance and Other Matters Based on an Engagement to Audit the Financial Statements Performed in Accordance with *Government Auditing Standards*

The Director of the Defense Logistics Agency and the
Inspector General of the Department of Defense

We were engaged to audit, in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States (*Government Auditing Standards)* and the provisions of Office of Management and Budget (OMB) Bulletin No. 24-01, *Audit Requirements for Federal Financial Statements,* the financial statements of the General Fund of the Defense Logistics Agency (DLA), which comprise the balance sheet as of September 30, 2023, and the related statements of net cost and changes in net position and combined statement of budgetary resources for the year then ended, and the related notes (collectively referred to as the "financial statements"), and have issued our report thereon dated November 8, 2023. Our report disclaims an opinion on the financial statements because DLA continues to have unresolved accounting issues and material weaknesses in internal controls that cause DLA to be unable to provide sufficient evidential support for complete and accurate financial statements on a timely basis.

## Report on Compliance and Other Matters

In connection with our engagement to audit the financial statements, we performed tests of DLA's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the financial statements, as well as the requirements referred to in the Federal Financial Management Improvement Act of 1996 (FFMIA). However, providing an opinion on compliance with those provisions was not an objective of our engagement, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and the provisions of OMB Bulletin No. 24-01, as described below. Additionally, if the scope of our work had been sufficient to enable us to express an opinion on the financial statements, other instances of noncompliance or other matters may have been identified and reported herein.

Our Report on Internal Control Over Financial Reporting dated November 8, 2023, includes additional information related to the financial management systems and internal controls that were found not to comply with the requirements, relevant facts pertaining to the noncompliance, and our recommendations to the specific issues presented.

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As referenced in the Fiscal Year (FY) 2023 DLA Statement of Assurance, DLA provides no assurance that the internal controls over operations, financial systems, reporting and compliance are operating effectively in compliance with the Federal Managers' Financial Integrity Act (FMFIA), Section 4; FFMIA of 1996, Section 803; and *Management's Responsibility for Enterprise Risk Management and Internal Control,* OMB Circular No. A-123 Appendix D.

**FFMIA**

Under FFMIA, we are required to report whether DLA's financial management systems substantially comply with federal financial management system requirements, applicable federal accounting standards, and the United States Standard General Ledger (USSGL) at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements. The results of the tests disclosed instances in which DLA's financial management systems did not substantially comply with federal financial management system requirements, applicable federal accounting standards or the USSGL.

(a) Federal financial management system requirements

EY identified as part of the Financial Information Systems material weakness, contained in the Report on Internal Control Over Financial Reporting, noncompliance with federal financial management system requirements for multiple systems. Weaknesses identified include those associated with user access, configuration management/change controls, segregation of duties, security management and IT operations. These financial system deficiencies prevent DLA from being compliant with federal financial management system requirements and inhibit DLA's ability to prepare complete and accurate financial reporting.

(b) Noncompliance with applicable federal accounting standards

As referenced in Note 1 to the financial statements, DLA self-identified that the design of their financial and nonfinancial systems does not allow DLA to comply with applicable federal accounting standards, including not being able to collect and record financial information as required by U.S. generally accepted accounting principles. EY also identified noncompliance with federal accounting standards during our testing, which was included in our Report on Internal Control Over Financial Reporting.

(c) Noncompliance with USSGL posting logic at the transaction level

EY also identified noncompliance with USSGL posting logic during our testing, which was included in our Report on Internal Control Over Financial Reporting.

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**FMFIA**

Federal Managers' Financial Integrity Act (FMFIA) of 1982 requires federal entities to establish internal controls, perform ongoing evaluations of the adequacy of the entity's system of internal control, and prepare related reports. The Government Accountability Office's (GAO's) *Standards for Internal Control in the Federal Government* (commonly referred to as the "GAO Green Book") issued under the authority of FMFIA, establishes five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communication and Monitoring. To determine if an entity's internal control system is effective, the Green Book requires management to assess the design, implementation and operating effectiveness of the five components of the entity's internal control system.

DLA has not implemented a formal internal control program that would allow it to substantially comply with FMFIA and the related GAO Green Book requirements, leading to inadequate control environment, risk assessment and monitoring processes.

DLA was not able to provide evidence that they are in compliance with significant aspects of OMB Circular A-123, which implemented FMFIA. DLA provided a FY 2023 Statement of Assurance, however there was not sufficient evidence that DLA fully completed an organizational risk assessment, identified relevant risks related to the financial statement assertions, documented the internal control standards as it relates to those assertions, performed internal control testing, and reported and tracked control deficiencies at the control level for each process identified. DLA provided evidence demonstrating that DLA has started to implement a testing strategy, however, DLA is unable to provide evidence that the extent of testing and review performed is sufficient to meet the requirements of FMFIA.

***DLA's Response to Findings***

*Government Auditing Standards* require the auditor to perform limited procedures on DLA's response to the findings identified in our engagement to audit and described in the accompanying Management's Response to the Audit Reports dated November 8, 2023. DLA's response was not subjected to the other auditing procedures applied in the engagement to audit the financial statements and, accordingly, we express no opinion on the response.

***Purpose of This Report***

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on the entity's compliance. This report is an integral part of an engagement to perform an audit in accordance with *Government Auditing Standards* in considering the entity's compliance. Accordingly, this communication is not suitable for any other purpose.

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**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2023 on our consideration of DLA's internal control over financial reporting. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and the results of that testing, and not to provide an opinion on the effectiveness of DLA's internal control over financial reporting. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DLA's internal control over financial reporting.

Ernst & Young LLP

November 8, 2023

# Management's Response to Audit Reports

DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD
FORT BELVOIR, VIRGINIA 22060-6221

MEMORANDUM FOR DEPARTMENT OF DEFENSE OFFICE OF THE INSPECTOR GENERAL

SUBJECT: Fiscal Year 2023 Financial Statement Audit

Thank you for the opportunity to comment on Ernst & Young, LLP's Independent Auditor Reports on the Defense Logistics Agency's (DLA) Fiscal Year (FY) 2023 financial statements. DLA remains fully committed to remediating audit findings, improving the accuracy of our financial data and reporting, and making progress towards unmodified audit opinions.

We continue to review audit findings from prior and current financial statement audits and are focused on remediating material weaknesses identified in Ernst & Young, LLP's Report on Internal Control over Financial Reporting. DLA will prioritize Agency requirements to address the scope limitations and align critical milestones within our Audit Roadmaps.

We appreciate Ernst & Young LLP due diligence during the FY 2023 audit. DLA reaffirms our commitment to achieving our audit goals within the Department in support of the Warfighter Always!

Susan J. Goodyear
Susan J. Goodyear
Director, DLA Finance
Chief Financial Officer

# Introduction to the DLA GF Principal Financial Statements

The DLA GF principal financial statements and the accompanying notes (financial statements) included in this report are prepared pursuant to the requirements of the CFO Act of 1990 (Pub. L. 101-576) and expanded by GMRA (Pub. L. 103-356) and other applicable legislation. Other reporting requirements include the OMB Circular A-136, as amended. The responsibility for the integrity of the financial information included in these financial statements rests with the management of DLA GF. The IPA was engaged to perform the audit of DLA GF's financial statements and disclaimed an opinion on these financial statements. The Audit Report, and Management's Response to the Audit Report, accompany the unaudited financial statements.

### The DLA GF financial statements consist of the following:

**The Balance Sheets** present those resources owned or managed by DLA GF that represent future economic benefits (assets), amounts owed by DLA GF that will require payments from those resources or future resources (liabilities), and residual amounts retained by DLA GF comprising the difference (net position) as of September 30, 2023 and 2022.

**The Statements of Net Cost** present the net cost of DLA GF operations for the years ended September 30, 2023 and 2022. DLA GF's net cost of operations is the gross cost incurred by DLA GF activities, less any exchange revenue earned and inter-entity eliminations from DLA GF activities.

**The Statements of Changes in Net Position** present the change in DLA GF's net position resulting from the net cost of DLA GF's operations, budgetary financing sources, and other financing sources for the years ended September 30, 2023 and 2022.

**The Combined Statements of Budgetary Resources** present how and in what amounts budgetary resources were made available to DLA GF, the status of these resources, and the net outlays of budgetary resources for the years ended September 30, 2023 and 2022.

**The Notes to the Principal Financial Statements** provide detail and clarification for amounts in the principal financial statements.

**Chinook Landing**
An Army CH-47 Chinook prepares to land on the flight deck of the USS Ronald Reagan in the Sea of Japan, Sept. 26, 2022. **Photo By:** Navy Petty Officer 3rd Class Gray Gibson

# Balance Sheets

As of September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 Restated |
|---|---|---|
| **ASSETS** | | |
| **Intragovernmental** | | |
| Fund Balance with Treasury (Note 2) | $ 2,251,314 | $ 2,406,663 |
| Accounts Receivable, Net (Note 3) | 14,768 | 13,779 |
| **Total Intragovernmental Assets** | **2,266,082** | **2,420,442** |
| **Other than Intragovernmental** | | |
| Accounts Receivable (Note 3) | 29 | 15 |
| Inventory and Related Property, Net (Note 4) | - | 29,486 |
| General Property, Plant and Equipment (Note 5) | 526,858 | 392,251 |
| Advances and Prepayments | 113,922 | 7,741 |
| Other Assets | 88 | 88 |
| **Total Other than Intragovernmental Assets** | **640,897** | **429,581** |
| **TOTAL ASSETS** | **$ 2,906,979** | **$ 2,850,023** |
| **LIABILITIES (Note 6)** | | |
| **Intragovernmental** | | |
| Accounts Payable | $ 19,262 | $ 21,418 |
| Other Liabilities: | | |
| Other Current Liabilities - Benefit Program Contributions Payable (Note 7) | 1,746 | 1,306 |
| Total Intragovernmental Other Liabilities | 1,746 | 1,306 |
| **Total Intragovernmental** | **21,008** | **22,724** |
| **Other than Intragovernmental** | | |
| Accounts Payable | 53,814 | 56,668 |
| Environmental and Disposal Liabilities (Note 8) | 76,446 | 78,346 |
| Federal Employee Benefits Payable (Note 7) | 9,155 | 8,041 |
| Advances from Others and Deferred Revenue | 23 | 24 |
| Other Liabilities (Note 9) | 3,817 | 3,102 |
| **Total Other than Intragovernmental Liabilities** | **143,255** | **146,181** |
| **TOTAL LIABILITIES** | **164,263** | **168,905** |
| **Commitments and Contingencies (Note 10)** | | |
| **NET POSITION** | | |
| Unexpended Appropriations - Funds from Other than Dedicated Collections | $ 2,296,782 | $ 2,344,480 |
| Cumulative Results of Operations - Funds from Other than Dedicated Collections | 445,934 | 336,638 |
| **TOTAL NET POSITION** | **2,742,716** | **2,681,118** |
| **TOTAL LIABILITIES AND NET POSITION** | **$ 2,906,979** | **$ 2,850,023** |

*The accompanying notes are an integral part of these statements.*

# Statements of Net Cost

For the Years Ended September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 Restated |
|---|---|---|
| **Operation and Maintenance** | | |
| Gross Cost | $ 437,432 | $ 420,406 |
| Less: Earned Revenue | (37,992) | (29,470) |
| **Net Cost** | **399,440** | **390,936** |
| **Procurement Defense-Wide** | | |
| Gross Cost | 16,107 | 9,902 |
| Less: Earned Revenue | - | - |
| **Net Cost** | **16,107** | **9,902** |
| **Research, Development, Test & Evaluation** | | |
| Gross Cost | 375,012 | 339,043 |
| Less: Earned Revenue | (38,206) | (49,328) |
| **Net Cost** | **336,806** | **289,715** |
| **Family Housing and Military Construction** | | |
| Gross Cost | 14,649 | 18,200 |
| Less: Earned Revenue | - | - |
| **Net Cost** | **14,649** | **18,200** |
| **Gross Cost** | **843,200** | **787,551** |
| **Less: Earned Revenue** | **(76,198)** | **(78,798)** |
| **NET COST OF OPERATIONS** | **$ 767,002** | **$ 708,753** |

*The accompanying notes are an integral part of these statements.*

# Statements of Changes in Net Position

For the Years Ended September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 Restated |
|---|---|---|
| **Unexpended Appropriations** | | |
| Beginning Balances | $ 2,344,480 | $ 1,883,232 |
| Appropriations Received | 1,035,743 | 1,419,418 |
| Appropriations Transferred-in/out | (12,049) | 1,779 |
| Other Adjustments | (19,081) | (29,861) |
| Appropriations Used | (1,052,311) | (930,088) |
| **Change in Unexpended Appropriations** | **(47,698)** | **461,248** |
| **Total Unexpended Appropriations: Ending Balance** | **2,296,782** | **2,344,480** |
| **Cumulative Results of Operations** | | |
| Beginning Balances | 336,638 | 521,106 |
| Correction of Errors | - | (50,127) |
| Beginning Balances, as Adjusted | 336,638 | 470,979 |
| Other Adjustments | 141 | (447) |
| Appropriations Used | 1,052,311 | 930,088 |
| Transfers-in/out Without Reimbursement | (180,700) | (358,018) |
| Imputed Financing | 4,546 | 2,789 |
| **Net Cost of Operations** | **767,002** | **708,753** |
| **Net Change in Cumulative Results of Operations** | **109,296** | **(134,341)** |
| **Cumulative Results of Operations: Ending Balance** | **445,934** | **336,638** |
| **TOTAL NET POSITION** | **$ 2,742,716** | **$ 2,681,118** |

*The accompanying notes are an integral part of these statements.*

# Combined Statements of Budgetary Resources

For the Years Ended September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 |
|---|---|---|
| **BUDGETARY RESOURCES** | | |
| Unobligated Balance from Prior Year Budget Authority, Net | $ 667,819 | $ 611,700 |
| Appropriations | 1,021,324 | 1,425,260 |
| Spending Authority from Offsetting Collections | 90,360 | 61,934 |
| **TOTAL BUDGETARY RESOURCES** | **$ 1,779,503** | **$ 2,098,894** |
| **STATUS OF BUDGETARY RESOURCES** | | |
| Total New Obligations and Upward Adjustments | $ 1,198,217 | $ 1,488,374 |
| Unobligated Balance, End of Year: | | |
| Apportioned, Unexpired Accounts | 497,218 | 567,259 |
| Unexpired Unobligated Balance, End of Year | 497,218 | 567,259 |
| Expired Unobligated Balance, End of Year | 84,068 | 43,261 |
| Total Unobligated Balance, End of Year | 581,286 | 610,520 |
| **TOTAL BUDGETARY RESOURCES** | **$ 1,779,503** | **$ 2,098,894** |
| **OUTLAYS, NET** | | |
| Outlays, Net | $ 1,160,102 | $ 912,204 |
| **AGENCY OUTLAYS, NET** | **$ 1,160,102** | **$ 912,204** |

*The accompanying notes are an integral part of these statements.*

# Notes to the Principal Financial Statements (Unaudited)

## Note 1: Summary of Significant Accounting Policies (Unaudited)

### A. Reporting Entity

Created in 1961, DLA is a component of the U.S. DoD and reports to the Office of the Under Secretary of Defense for Acquisition and Sustainment through the Assistant Secretary of Defense for Sustainment. DLA provides materials and services to components of DoD (including the U.S. Army, Navy, and Air Force, Marine Corps and Space Force), other Federal agencies, and public entities. DLA accomplishes its mission and goals through the operations of the DLA WCF, DLA GF, and DLA NDSTF. These financial statements and accompanying notes herein only refer to the activities of DLA GF.

Congress annually appropriates DLA GF amounts to DLA, which also grants authority to the OUSD and its Components to obligate those funds to support mission requirements. In FY 2023 and FY 2022, DLA GF received four appropriations, which include O&M, RDT&E, PDW, and MILCON.

### B. Basis of Presentation and Accounting

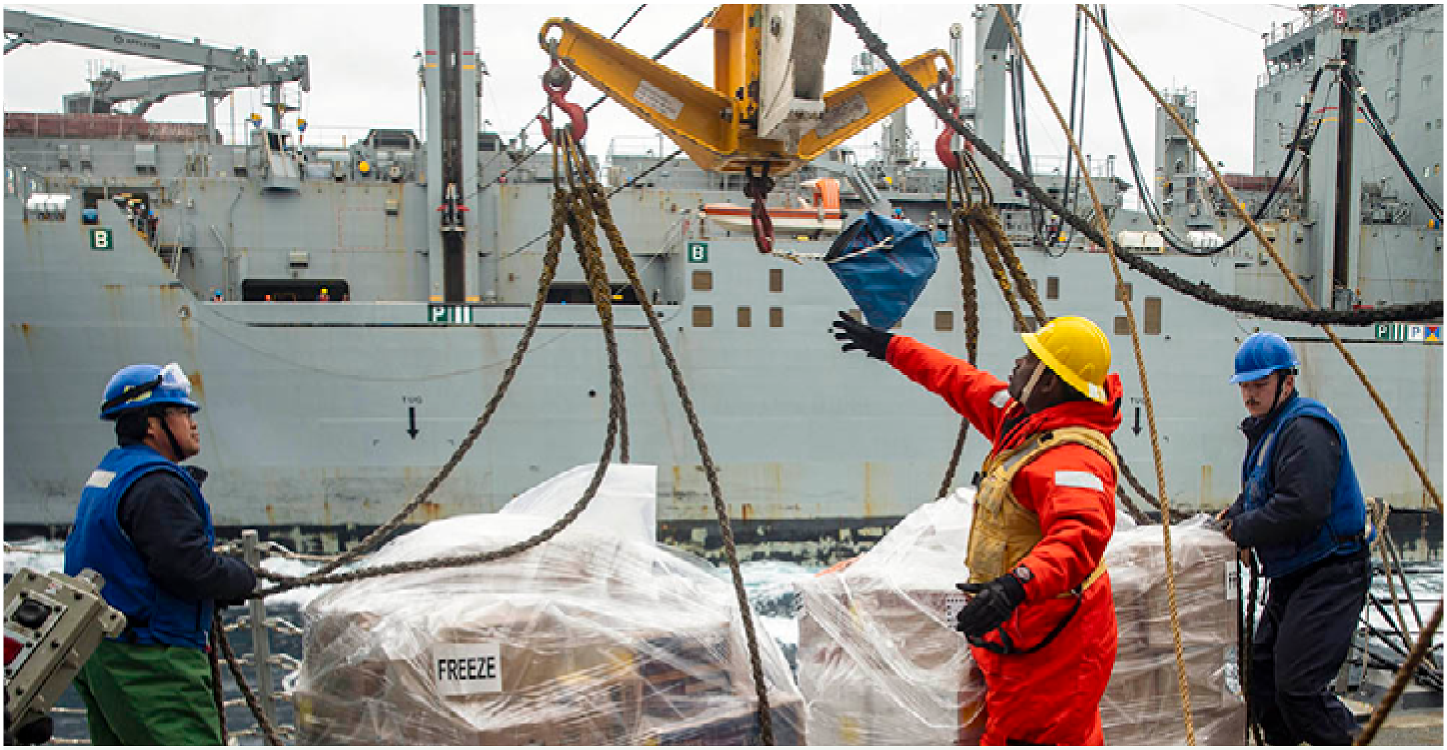
**Basis of Presentation and Accounting:** The DLA GF fiscal year ends September 30. The accompanying financial statements account for all resources for which DLA GF is responsible. These financial statements present the financial position, results of operations, changes in net position, and the combined budgetary resources of DLA GF, as required by the CFO Act of 1990, expanded by the GMRA of 1994, and other applicable legislation. The financial statements are prepared from the books and records of DLA GF activities, in accordance with U.S. GAAP, promulgated by the FASAB[9], and presented in the format prescribed by the OMB Circular A-136, except as identified in Note 1.C., *Departures from U.S. GAAP*, and in the following paragraphs.

The DLA GF financial statements reflect both accrual and budgetary accounting transactions, except as identified in Note 1.C., *Departures from U.S. GAAP*. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when incurred, without regard to the receipt or payment of cash. Budgetary accounting is based on concepts set forth by OMB Circular A-11, *Preparation, Submission, and Execution of the Budget*, as amended which provides instructions on budget execution. Budgetary accounting is designed to recognize the budgetary resources and the related status of those budgetary resources, including the obligation and outlay of funds according to legal requirements, which in many cases is made prior to the occurrence of an accrual-based transaction. Budgetary accounting is essential for compliance with legal constraints and controls over the use of Federal funds.

The DLA GF is unable to fully prepare financial statements in conformity with and implement all elements of U.S. GAAP (refer to Note 1.C., *Departures from U.S. GAAP*), the form and content requirements for Federal government entities specified by OMB Circular A-136, due to limitations of financial and nonfinancial management processes and systems that support the financial statements. In addition, the financial management systems used by DLA GF are unable to meet all full accrual and budgetary accounting requirements as many of the financial and nonfinancial feeder systems and processes were not designed to collect and record financial information on the full accrual accounting basis as required by U.S. GAAP. These systems were designed to support reporting requirements for maintaining accountability over assets, reporting the status of Federal appropriations, and recording information on a budgetary basis, rather than preparing financial statements in accordance with U.S. GAAP.

Therefore, DLA GF is continuing the necessary actions required to bring its financial and nonfinancial systems and processes to generate financial statements and the accompanying notes in accordance with U.S. GAAP and in compliance with the reporting requirements of OMB Circular A-136. DLA is assessing financial feeder systems and processes and their conformance to existence, completeness, and accuracy requirements as required by U.S. GAAP and OMB Circular

[9] FASAB is the official body for setting accounting standards of the U.S. government




**Sea Delivery**

Sailors aboard the USS John Finn receive a pallet of cargo during a replenishment with the USNS Wally Schirra in the Pacific Ocean, May 13, 2023. **Photo By:** Navy Petty Officer 2nd Class Samantha Oblander

A-136. As DLA GF identifies non-conforming data issues, the Agency will continue to implement interim mitigation processes to address these limitations. In addition, DLA GF is remediating material weaknesses found in all end-to-end business process cycles pertaining to reconciliations and adequacy of the supporting documentation identified through audits and other compliance reporting.

**Combined Statements of Budgetary Resources:** The budgetary accounting concepts are recognized in the Combined Statements of Budgetary Resources. The Combined Statements of Budgetary Resources present: (1) budgetary resources for the fiscal year; (2) status of those budgetary resources (includes obligated[10] amounts and unobligated[11] amounts for the fiscal year); and (3) Outlays[12], Net for the fiscal year, which is comprised of Outlays less Actual Offsetting Receipts (cash transactions). DLA GF's budgetary resources[13] include unobligated balances of resources from prior years and new resources, consisting of appropriations and spending authority from offsetting collections.

**Intragovernmental and Other than Intragovernmental Transactions:** SFFAS 1, *Accounting for Selected Assets and Liabilities*, distinguishes between Intragovernmental and Other than Intragovernmental assets and liabilities. Intragovernmental assets and liabilities arise from transactions among Federal entities. Intragovernmental assets are claims other Federal entities owe to DLA GF. Intragovernmental liabilities are claims DLA GF owes to other Federal entities. Whereas Other than Intragovernmental assets and liabilities arise from transactions with public entities. The term "public entities" encompasses domestic and foreign persons and or-

[10] Per OMB Circular A-11, Section 20, " Obligated amount means a legally binding agreement that will result in outlays, immediately or in the future."

[11] Per OMB Circular A-11 , Section 20, " Unobligated amount means the cumulative amount of budget authority that remains available for obligation under law in unexpired accounts.

[12] Per OMB Circular A-11, Section 20, " Outlay means a payment to liquidate an obligation (other than the repayment to the Treasury of debt principal)... Outlays are a measure of Government spending."

[13] Per OMB Circular A-11 , Section 20, " Budgetary resources are amounts available to incur obligations in a given year. Budgetary resources consist of new budget authority and unobligated balances of budget authority provided in previous years."

ganizations outside the U.S. Government. Other than Intragovernmental assets are claims of DLA GF against public entities. Other than Intragovernmental liabilities are amounts that DLA GF owes to public entities. Currently, DLA GF is unable to accurately map its trading partners to separate Intragovernmental and Other than Intragovernmental transactions in accordance with TFM, Volume I, Part 2, Central Accounting and Reporting, Chapter 4700, *Federal Entity Reporting Requirements for the Financial Report of the United States Government*.

The DLA GF engages in transactions with other DoD and Federal entities that generate inter-DoD and intragovernmental balances; however, DLA GF is unable to reconcile and resolve differences between balances and transactions with other DoD and Federal entities in accordance with OMB Circular A-136 requirements and TFM 4700 guidance. The reconciliation process is not fully implemented.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions.)

**Intra-departmental Transactions:** DLA GF is ultimately responsible for the accuracy of its trading partner data and initiating actions to reconcile balances with its trading partners; however, DLA GF is unable to resolve the reconciling differences in amounts reported for the buyer/seller transactions reciprocal category with ODOs. A DoD reporting entity unable to provide detail transactions at the appropriate time of the financial statement reporting cycle must adjust its balance to match the seller's or buyer's supportable data (refer to Note 1.C., *Departures from U.S. GAAP*, related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions).

**Inter-fund Transactions:** Inter-fund transactions and balances among DLA GF appropriations are eliminated from the Balance Sheets, the Statements of Net Cost, and the Statements of Changes in Net Position. The Combined Statements of Budgetary Resources are presented on a combined basis in accordance with OMB Circular A-136; therefore, inter-fund transactions have not been eliminated from these statements. DLA GF presents the Statements of Net Cost based on appropriations rather than program costs, which is not in accordance with OMB Circular A-136 (refer to Note 1.C., *Departures from U.S. GAAP*, related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions and Statements of Net Cost).

**Classified Activities:** Accounting standards require all reporting entities to disclose that accounting standards allow certain presentations and disclosures to be modified, if needed, to prevent the disclosure of classified information.

**Use of Estimates:** The DLA GF management has made certain estimates and assumptions when reporting assets, liabilities, revenue, and expenses and disclosures in the notes. Uncertainties associated with these estimates exist and actual results may differ from these estimates; however, DLA GF's estimates are based on historical experience, current events and other assumptions that are believed to be reasonable under the circumstances. Significant estimates reported in the financial statements include: (1) E&DL; (2) accounts payable accrual; (3) undelivered orders; and (4) FECA actuarial liability as of the date of these financial statements.

## C. Departures from U.S. GAAP

Financial management systems and operations continue to be evaluated and modified as DLA GF strives to remediate its material weaknesses and record and report its financial activity in accordance with U.S. GAAP. Therefore, DLA GF is determining the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with U.S. GAAP. However, due to the financial management systems and operational limitations, the known departures from U.S. GAAP described below that impact DLA GF financial statements have been identified although other departures from U.S. GAAP may exist that have not been identified.

**Definition of Reporting Entity (Note 1.A.):** The DLA GF has not completed analyzing material applicable business relationships with other organizations to identify consolidation entities, disclosure entities, or related parties in accordance with SFFAS 47, Reporting Entity (effective FY 2018). As a result, DLA GF is unable to determine if there are consolidation entities that are required to be consolidated and disclosed in DLA GF financial statements or disclosure entities and related parties, where the nature and magnitude of such relationships, are required to be disclosed in a Disclosure Entities and Related Parties note to the financial statements.

**Statements of Net Cost:** The DLA GF does not have policies and compliant processes in place to present its major program costs aligned with DLA GF mission and goals by responsibility segments in accordance with SFFAS 4, *Managerial Cost Accounting Concepts and Standards*, and OMB Circular A-136.

**Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions (Note 1.B.):** The DLA GF does not have compliant processes in place to properly report and distinguish between intragovernmental, intra-departmental, and Other than Intragovernmental transactions in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*.

**Inter-Entity Cost (Note 1.S.):** The DLA GF does not have compliant processes in place to recognize all significant inter-entity costs related to inputs of its goods or services provided to entities for a fee or user charge in accordance with SFFAS 55, *Amending Inter-Entity Cost Provisions* (effective FY 2019). Generally, the fees and user charges should recover the full costs of those goods and services. Thus, the cost of inter-entity goods or services needs to be recognized by the receiving entity in order to determine fees or user charges for goods and services sold.

**Fund Balance with Treasury (Note 1.F. and Note 2):** The DLA GF is not able to account for Fund Balance with Treasury in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, due to its inability to identify and reconcile the reported differences between DLA GF's accounting system and Treasury. Monthly unsupported journal vouchers are made to adjust the Fund Balance with Treasury balances in DLA GF financial statements to match U.S. Treasury records.

**Accounts Receivable, Revenue, and Unfilled Customer Orders (Notes 1.G., 1.S. and Note 3):** The DLA GF does not have policies and compliant processes in place to: (1) recognize revenue and record the related accounts receivable, net and UCO balances from goods sold and services provided in the proper period; (2) identify, evaluate, record, and report an allowance for doubtful accounts related to intragovernmental receivables in accordance with SFFAS 1 and Technical Bulletin 2020-1, *Loss Allowance for Intragovernmental Receivables*; and (3) adjust revenue to the extent that realization of the full amount is not probable in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, and/or SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*.

**Inventory and Related Property, Net (Note 1.H. and Note 4):** The DLA GF does not have policies and compliant processes in place to properly evaluate, record, and report Inventory and Related Property, Net in accordance with SFFAS 3, *Accounting for Inventory and Related Property*. More specifically DLA GF does not have proper policies and compliant processes: 1) to support the valuation of inventory; 2) to support when goods/services are received; and 3) to determine the category of inventory in accordance with SFFAS 3, *Accounting for Inventory and Related Property*.

**General Property, Plant and Equipment, Net (Note 1.I. and Note 5):** The DLA GF does not have policies and compliant processes in place to account for general PP&E at historical cost, in accordance with SFFAS 6, A*ccounting for Property, Plant, and Equipment*, and SFFAS 10, *Accounting for Internal Use Software*. Supportable general PP&E beginning balances have not been established CIP, IUS, and IUS in Development using the alternative valuation methods permitted by SFFAS 50, *Establishing Opening Balances for General Property, Plant, and Equipment* (effective FY 2017). In addition, DLA GF does not have compliant processes in place to account for impairment of facilities and equipment in accordance with SFFAS 44, *Accounting for Impairment of General Property, Plant, and Equipment Remaining in Use*. More specifically:

Construction-in-Progress Balances: The DLA GF does not have the proper policies and compliant processes to identify aged CIP balances in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment*. In addition, DLA GF does not have policies and compliant processes in place to properly monitor and reconcile CIP transactions in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipmen*t, as a result of a system migration;

Internal Use Software and Internal Use Software in Development: The DLA GF does not have the proper policies and compliant processes to identify IUS in Development balances in accordance with SFFAS 10, *Accounting for Internal Use Software* (refer to Note 13, *Restatement*);

Capitalization Thresholds: The DLA GF does not have policies and procedures to implement and consistently apply capitalization thresholds in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment*, and SFFAS 10, *Accounting for Internal Use Software*;

Depreciation: The DLA GF does not properly follow the policies and procedures to effectively implement and consistently apply depreciation and amortization, in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment*, and SFFAS 10, *Accounting for Internal Use Software*; and

Rights and Obligations: The DLA GF is unable to substantiate whether DLA WCF has the rights and obligations to the recorded general PP&E assets in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment*.

**Advances and Prepayments (Note 1.K.):** The DLA GF does not have policies and compliant processes in place to record advances and prepayments related to contract financing payments in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*.

**Leases (Note 1.J. and Note 5):** The DLA GF does not have policies and compliant processes in place and has not performed an analysis to identify, evaluate, record, and report capital and operating leases in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*, SFFAS 6, *Accounting for Property, Plant, and Equipment*, and SFFAS 10, *Accounting for Internal Use Software*. As such, DLA GF does not have any capital or operating leases reported or disclosed as of September 30, 2023 and 2022.

**Accounts Payable, Expenses, and UDO (Notes 1.M. and 1.T.; Notes 6; Note 9; and Note 11):** The DLA GF does not have policies and compliant processes in place to account for accounts payable, expense accruals, and the related UDOs in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, and SFFAS 5, *Accounting for Liabilities of The Federal Government*. More specifically:

Negative Payable: The DLA GF processes allow for payment without receipt, thus resulting in a negative payable. This occurs when a payment is made prior to the goods receipts being posted in DLA GF's accounting system. This results in a misstatement of current year expenses and payables, and a corresponding misstatement of UDOs;

Undelivered Orders: The DLA GF does not have sufficient policies and procedures in place to record obligations at the time contracts are awarded in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*. In addition, DLA GF is unable to support the UDO balance in the accounting system;

Right of Offsets: The DLA GF does not have policies and compliant procedures in place to evaluate whether a right of offsets exist within the contract agreements that will allow DLA to properly recognize assets and liabilities in accordance with Financial Accounting Standards Board Accounting Standards Codification 210.20, *Balance Sheet-Off Setting*, as prescribed by SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*; and

**Environmental and Disposal Liabilities (Note 1.N. and Note 10):** The DLA GF does not have policies and compliant processes in place to reconcile asset listings for costs related to cleanup, asset closure, and asbestos associated with general PP&E, in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*; SFFAS 6, *Accounting for Property, Plant, and Equipment*; and Federal Financial Accounting and Auditing Technical Release 2, *Determining Probable and Reasonably Estimable for Environmental Liabilities* in the Federal Government.

**Commitments and Contingencies (Note 1.L. and Note 10):** The DLA GF did not complete its assessment of commitments and contingencies in accordance with SFFAS 5, *Accounting for Liabilities of The Federal Government*, and SFFAS 12, *Recognition of Contingent Liabilities Arising from Litigation: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government*.

**Reconciliation of Net Cost to Net Outlays (Note 12):** The DLA GF does not have an established policy for the reconciliation of net cost to net outlays in accordance with SFFAS 53, *Budget and Accrual Reconciliation*. DLA GF is also unable to fully prepare the reconciliation of net cost to net outlays in conformity with U.S. GAAP due to limitations of financial and nonfinancial management processes and systems that support the underlying financial information.

**Public-Private Partnerships:** The DLA GF has not completed analyzing all the applicable business relationships to determine if these arrangements or transactions indicate the existence of P3 relationships, risk-sharing arrangements or transactions lasting more than five years between public and private sector entities, in accordance with SFFAS 49, *Public-Private Partnerships: Disclosure Requirements* (effective FY 2019). As a result, DLA GF is unable to determine the nature of such partnerships, if applicable, and related Federal funding amounts required to be disclosed in a P3 note to the financial statements.

## D. Pronouncements Recently Issued but Not Yet Effective

FASAB has issued the following pronouncements that may affect future financial presentation, as well as financial management practices and operations of DLA GF upon implementation. DLA GF has not completed the process of evaluating the effects of adopting these pronouncements and is unable to determine the materiality of changes that adopting them will have on its financial position, results of operations, changes in net position, and combined budgetary activity.

| FASAB Statement No. | SFFAS 54 | SFFAS 57 (paragraphs 3 – 8, 11, and 12) | SFFAS 60 | SFFAS 61 |
|---|---|---|---|---|
| FASAB Standard | Leases: An Amendment of SFFAS 5, *Accounting for Liabilities of the Federal Government*, and SFFAS 6, *Accounting of Property*, *Plant*, *and Equipment* | Omnibus Amendments FY 2019 | Omnibus Amendments FY 2021 | Omnibus Amendments FY 2023 |
| Adoption Required in FY | Deferred to FY 2024 | Effective FY 2024 | Effective FY 2024 | Effective FY 2024 |

SFFAS 58, *Deferral of the Effective Date of SFFAS 54*, Leases, defers SFFAS 54, *Leases: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government, and SFFAS 6, Accounting for Property, Plant, and Equipment*, until FY 2024; earlier implementation is not permitted. SFFAS 54, revised the current Federal financial reporting standards for lease accounting and requires that Federal lessees recognize a lease liability and a leased asset at the commencement of the lease term, unless it meets any of the scope exclusions or the definition/criteria of short-term leases, or contracts or agreements that transfer ownership, or intragovernmental leases. SFFAS 57, *Omnibus Amendments 2019*, SFFAS 60, *Omnibus Amendments 2021: Leases-Related Topic*s, and SFFAS 61, *Omnibus Amendments 2023:Leases-Related Topics II*, amend certain references to leases affected by SFFAS 54, as well as other minor changes in order to improve clarity of existing statements.

## E. Appropriations and Funding

The DLA GF receives allotted funding through the annual appropriations received by the OUSD(C). DoD's annual appropriations are apportioned by OMB. Apportionment is part of the government-wide system for the administrative control of funds. Unless expressly exempted or automatically apportioned by OMB, all DoD appropriated, collected, and recovered resources require OMB approval through the apportionment/reapportionment process before they are available for distribution and legal obligation by OUSD(C). Following the approval of apportionment/reapportionment requests by OMB, OUSD(C) allocates funds to the Military Services and ODOs. Funds distributed by OUSD(C) may be further subdivided through sub-allocation and sub-allotment to lower levels within the organizations or across organizations for execution.

The DLA GF receives its budgetary resources through sub-allotments from OUSD(C). These sub-allotments received by the DLA GF annually are reported in the Statements of Budgetary Resources and included in the appropriations line as part of DLA GF's budgetary resources. These budgetary resources provide the funding necessary to incur obligations, pay for goods and services, and are available for obligations based on the period of availability as described below. Any budgetary resources remaining at the end of the period of availability are held in 'an expired status' for five years. Existing obligated balances can be used to make payments, but unobligated balances are not available for new obligations. Budgetary resources, including any related obligations and payables, are cancelled at the end of the five-year expiration period.

**O&M appropriation (funds available year(s) 1 year):** funds Administration and Service-Wide Activities such as DoD programs, DoD EBS, DLA HQ programs, and Environmental Programs. These programs are associated with DLA logistics mission as well as programs assigned to DLA GF from DoD for budget administration purposes. DLA GF functions as either the executive agent responsible for program oversight and policy guidance or the budget administrator responsible for administrative support for these programs.

**Procurement Defense-Wide appropriation (funds available year(s) 3 years):** funds 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 GF's logistics mission.

**RDT&E appropriation (funds available year(s) 2 years):** funds the development of major upgrades to increase the performance of existing systems, the purchase of test articles, and the developmental testing and/or initial operational testing and evaluation prior to system acceptance. In addition, the RDT&E appropriation develops, manages, and implements innovative microelectronic solutions to enhance DoD mission capabilities. These capabilities are leveraged to develop low-volume, high mix fabrication processes for state-of-the-art technologies that meet DoD's performance and reliability needs for legacy microelectronics that are unavailable from commercial foundries. RDT&E also helps ensure that advanced logistics concepts and business processes are used to accomplish the Agency's mission. The Logistics R&D program identifies the best commercial business practices and tailors them, as necessary, into the most effective business processes for DLA. The ManTech R&D program provides the critical link between invention and application. DLA sub-allots RDT&E authority to the DMEA.

### Family Housing and Military Construction

**Family Housing O&M appropriation (funds available year(s) 1 year):** funds the routine O&M of 24 Military Family Housing (MFH) units. Routine operation and maintenance include management costs, utility costs and cyclical maintenance such as painting and renovations. Allocated funding for Family Housing ended in FY 2019, all remaining obligated and unobligated balances will be cancelled by FY 2025.

**MILCON appropriation (funds available year(s) 5 years):** funds the construction of facilities that support DLA's mission. These include DoD fuel infrastructure projects, and distribution and disposition facilities. DLA GF sub-allots MILCON authority to various entities such as USACE and NAVFAC, which are DLA's primary design and construction agents for the MILCON program.

## F. Fund Balance with Treasury

The DLA GF does not maintain cash in a commercial bank, but rather in the U.S. Treasury. DLA GF's FBwT includes the amount available for DLA GF to pay current liabilities and finance authorized purchases, except as restricted by law. The disbursing offices of DFAS, USACE, GSA, and the Department of State's financial service centers process DLA GF's cash collections, disbursements, and adjustments.

In recent years, DLA GF implemented U.S. TDD, which provides DLA GF the capability to transmit directly from the accounting system to Treasury for disbursements. With the implementation of TDD, DLA GF has a unique accounting code, which allows DLA GF to properly identify the transactions.

On a monthly basis, DLA GF adjusts the FBwT account balance to bring the cash balance to be in agreement with the U.S. Treasury cash balance reported on the Central Accounting and Reporting System (CARS) using the CMR. The CMR provides a summary cash position for each ODO's FBwT account by fiscal year and appropriation at the limit level. The adjustments represent the undistributed disbursements and collections amounts that have been reported to U.S. Treasury, but have not yet been posted to DLA GF's accounting system. Undistributed amounts can be a result of timing, invalid line of accounting, invalid TAS information, and unsupported and unreconciled differences.

The DLA GF's accounting service provider, DFAS, uses U.S. Treasury suspense accounts to hold transactions temporarily prior to identifying the correct appropriation. Suspense account items represent the amounts that are reported to Treasury at the TI Level (TI-17, TI-21, TI-57, TI-97), but have not yet been classified to a DLA GF TAS. The transactions in suspense accounts include unidentified collections, disbursements, and Intragovernmental Payment and Collection transactions at month end. DFAS research suspense transactions in each TI to post them against the appropriate line of accounting. The current balances for DLA GF suspense transactions are derived from the DFAS Suspense Account UoT.

U.S. Treasury also compares DoD's FBwT reported by DFAS with comparable data submitted by financial institutions and Treasury Regional Financial Centers and notifies DoD of differences in collection and disbursement data on the SOD report. DFAS reviews the SOD report to research and resolve differences. The current balances for DLA GF SOD transactions are derived from DFAS management analysis and the SOD UoT.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Fund Balance with Treasury, and Note 2, *Fund Balance with Treasury*.)

## G. Accounts Receivable, Net

Accounts Receivable represent amounts due to DLA GF by other Federal agencies (intragovernmental) and the public (other than intragovernmental). DLA GF's accounts receivable arise from sales of materials and services.

The DLA GF presents its intragovernmental accounts receivable net of an allowance for doubtful accounts, which is based on a systematic methodology of grouped aged Federal accounts receivables. DLA GF evaluates the allowance methodology and estimates allowance percentages quarterly based on historical average collections on aged Federal accounts receivables. The allowance for doubtful accounts is calculated based on the aged accounts receivable balances from the preceding month.

The DLA GF does not currently have significant other than intragovernmental receivables or corresponding allowance for doubtful accounts

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Net, Revenue, and Unfilled Customer Orders.)

**DLA Encourages Open Communication with Industry Partners**

Defense Logistics Agency Director Navy Vice Adm. Michelle Skubic speaks to the attendees at the Agency's Industry Association Meeting, held April 25, 2023, at the McNamara Headquarters Complex at Fort Belvoir, Virginia. The Agency provided an update on its demand forecast and most recent supplier survey during the meeting, and there were discussions between the Agency and the industry associations that attended. **Photo By:** Christopher Lynch

## H. Inventory and Related Property, Net

Inventory and Related Property, Net consist of the inventory held-for-sale related to the acquisition of equipment to support the PDW program. Per DoD Financial Management Regulations (FMR) 7000.14-R Volume 4, Chapter 4, Inventory and Related Property, DLA GF should not hold inventory . In FY 2023, all DLA GF inventory held-for-sale was transferred to DLA WCF.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to *Inventory and Related Property.*)

## I. General Property, Plant and Equipment, Net

The DLA GF PP&E primarily consists of Real Property CIP, IUS and IUS under development. These PP&E categories are not subject to amortization or depreciation. DLA GF PP&E also consists of IUS and General Equipment.

The DLA GF transfers the amounts in the CIP account to the DLA WCF upon project completion. DLA WCF will place assets in the appropriate PP&E account and transfer the asset to the military services. Due to identified deficiencies in policies and procedures related to CIP, DLA GF is not able to reconcile the recorded CIP balances.

**Capitalization Threshold:** The DLA GF general PP&E assets are recorded at historical acquisition cost plus improvements when an asset has a useful life of two or more years, and the acquisition cost exceeds the $250,000 capitalization threshold.

The DLA GF determines the useful life of its general PP&E using the asset classification and the type of assets based on the DoD FMR 7000.14-R Volume 4, Chapters 24, 25, 27 and the OUSD Memorandum "Financial Reporting Policy for Real Property Estimated Useful Lives, Land Valuation, and Accounting for Real Property Outside of the United States."

The DLA GF has not yet finalized the valuation process for PP&E. Accordingly, DLA GF has not made an unreserved assertion that the opening balances of PP&E for FY 2023 are presented fairly in accordance with SFFAS 50, *Establishing Opening Balances for General Property, Plant, and Equipment.*

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to General Property, Plant and Equipment, Net, and Note 5, *General Property, Plant and Equipment*, and Note 13, *Restatements*)

### Depreciation Method and Useful Life

| Asset Classes | Depreciation/ Amortization Method | Useful Life (Years) |
|---|---|---|
| IUS | Straight-line | 2, 5 or 10 |
| General Equipment | Straight-line | 5 or 10 |
| CIP | Not Applicable | Not Applicable |
| IUS in development | Not Applicable | Not Applicable |

## J. Leases

As of the date of these financial statements, DLA GF has not completed the process of developing policies and procedures to identify, calculate, record and report capital and operating leases in accordance with SFFAS 5, *Accounting for Liabilities of The Federal Government*, and SFFAS 6, *Accounting for Property, Plant, and Equipment* (refer to Note 1.C., *Departures from U.S. GAAP*, related to Leases).

## K. Advances and Prepayments

Advances represent cash outlays to cover a part or all of the recipients' anticipated expenses or as advance payments for the cost of goods and services the entity acquires. Prepayments represent payments made by a federal entity to cover certain periodic expenses before those expenses are incurred.

The DLA GF conducts business with 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 GF provides the following contract financing payments: commercial financing payments, progress payments, and performance-based payments. The Federal Acquisition Regulation, Part 32, defines contract financing payments as "authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government". Advances are reduced when goods or services are received, contract terms are met, or progress is made under a contract.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Advances and Prepayments.)

## L. Commitments and Contingencies

In accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*, as amended by SFFAS 12, *Recognition of Contingent Liabilities Arising from Litigation: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government,* DLA GF evaluates all contingent liabilities based on three criteria: probable, reasonably possible, and remote. DLA GF recognizes contingent liabilities in DLA GF's Balance Sheets and Statements of Net Cost when the loss is determined to be probable and reasonably estimable. DLA GF discloses those contingencies that are reasonably possible in Note 10, *Commitments and Contingencies.* DLA GF does not disclose or record contingent liabilities when the loss is considered remote.

The DLA GF recognizes that the estimated liability may be a specific amount or a range of amounts. If an amount within the range is a better estimate than any other amount within the range, that amount is recorded. If no amount within the range is a better estimate than any other amount, the minimum amount of the range is recorded and the range and a description of the nature of the contingency are disclosed.

In the event of an adverse judgment against the Government, some of the legal contingent liabilities may be payable from the U.S. Treasury. For legal contingency matters where DLA Counsel is unable to express an opinion regarding the likely outcome of the case and an estimate of the potential liability cannot be made, the total amount claimed against the government is classified as "Reasonably Possible" and disclosed if available.

The DLA GF records an accrual for and discloses probable E&DL contingencies in Note 10, *Commitments and Contingencies*.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities and Commitments and Contingencies; Note 8, *Environmental and Disposal Liabilities*; and Note 10, *Commitments and Contingencies*)

## M. Liabilities

Liabilities represent probable and measurable future outflows of resources as a result of past transactions or events and are recognized when incurred, regardless of whether there are budgetary resources available to pay the liabilities. However, liabilities cannot be liquidated without legislation providing resources and legal authority.

**Liabilities Covered and Not Covered by Budgetary Resources:** Liabilities covered by budgetary resources include those liabilities for which Congress appropriated funds and are otherwise available to pay amounts due as of the Balance Sheet dates. Liabilities Not Covered by Budgetary Resources are liabilities that will require budgetary resources and are amounts owed in excess of available, congressionally appropriated funds. Therefore, no budgetary resources are available to pay amounts due as of the Balance Sheet dates but will require future funding to liquidate the obligation (refer to Note 6, *Liabilities Not Covered by Budgetary Resources*).

**Current and Noncurrent Liabilities:** The DLA GF discloses its other liabilities between current and noncurrent liabilities in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*. Current liabilities represent liabilities that DLA GF expects to settle within 12 months of the Balance Sheet dates. Noncurrent liabilities represent liabilities that DLA GF does not expect to be settled within 12 months of the Balance Sheet dates (refer to Note 9, *Other Liabilities*).

**Accounts Payable:** Accounts Payable includes amounts owed but not yet paid to Intragovernmental and Other than Intragovernmental entities for goods and services received by DLA GF. DLA GF estimates and records accruals when services and goods are performed or received (i.e., MOCAS accrual) related to contract financing and Negative Payable Accrual to adjust the timing issues that exist within EBS when an invoice is received and posted without a goods receipt. DLA GF also accrues liabilities incurred at month-end but not yet recorded using data from Third Party Payment Systems, GPC, various feeder systems, and estimates of costs incurred when goods or services received but not invoiced. For Accounts Payable associated with cancelling appropriations, the cancelled payable is re-established after funding expired and are no longer available to liquidate obligations. The payments for the cancelled payable will be disbursed using current available funding (refer to Note 6, *Liabilities Not Covered by Budgetary Resources*).

**Advances from Others and Deferred Revenue:** Advances from Others and Deferred Revenue are cash received in advance of goods or services that have not been fully rendered.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses and Undelivered Orders).

## N. Environmental and Disposal Liabilities

E&DL are a probable and reasonably estimable future outflow or expenditure of resources that exists as of the financial reporting date for environmental cleanup costs resulting from past transactions or events.

The DLA GF is responsible for accurate reporting of the E&DL and expense for the real property and/or equipment that it records and reports in its financial statements as assets, regardless of ownership by any Federal agency. DLA GF identifies and estimates accrued E&DL through its annual CTC process. DLA GF accrued E&DL comprises of environmental cleanup costs associated with restoration of environmental sites on real property that it does not own but has received appropriated funds to execute and manage. These environmental sites may include, but are not limited to, decontamination, decommissioning, site restoration, site monitoring, clean closure of assets, and post-closure costs related to the Agency's operations that result in hazardous waste. Due to noted deficiencies, DLA GF is not able to reconcile the population of real property assets that encompass the environmental sites closure and asbestos liabilities.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities and Commitments and Contingencies, Note 8, *Environmental and Disposal Liabilities,* Note 10, *Commitments and Contingencies,* and Note 13, *Restatement*.)

## O. Payroll and Leave Accruals

Accrued payroll consists of salaries, wages, and other compensation earned by employees, but have not yet been disbursed as of the Balance Sheets dates. DLA GF accrues the cost of unused annual leave, including restored leave, compensatory time, and credit hours as earned and reduces the accrual when leave is taken. The payroll and annual leave accrual liability is accrued based on the latest pay period data for reporting purposes (refer to Note 9, *Other Liabilities*).

## P. Federal Employee Benefits Payable

The FECA (Public Law 103-3) provides income and medical cost protection to covered Federal civilian employees injured on the job, to employees who have incurred work-related occupational diseases, and to beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. The FECA program is administered by DOL, which pays valid claims and subsequently seeks reimbursement from DLA GF for these paid claims. The FECA liability consists of two elements.

The first element, accrued FECA liability, is based on actual future payments for claims paid by DOL but not yet reimbursed by DLA GF. DLA GF reimburses DOL for claims as funds are appropriated for this purpose. In general, there is a one to two-year period between payment by DOL and reimbursement to DOL by DLA GF. As a result, DLA GF recognizes an intra-governmental liability, not covered by budgetary resources, for the claims paid by DOL that will be reimbursed by DLA GF (refer to Note 6, *Liabilities Not Covered by Budgetary Resources*, and Note 7, *Federal Employee Benefits Payable and Related Other Liabilities*).

The second element, actuarial FECA liability, is the estimated liability for future payments and is recorded as a liability Other than Intragovernmental, not covered by budgetary resources. The actuarial FECA liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. DOL determines the actuarial FECA liability annually, as of September 30, using an actuarial method that considers historical benefit payment patterns, wage inflation factors, medical inflation factors, and other variables. The projected annual benefit payments are discounted to present value. The methodology for billable projected liabilities includes: (1) an algorithmic model that relies on individual case characteristics and benefit payments (the FECA Case Reserve Model); and (2) incurred but not reported claims were estimated using historical incurred benefit liabilities and payments (refer to Note 6, Liabilities Not Covered by Budgetary Resources, and Note 7, *Federal Employee Benefits Payable and Related Other Liabilities*).

## Q. Pension Benefits

Based on the effective Federal government start date, the DLA GF's civilian employees participate in either the CSRS, a defined benefit plan, or the FERS, a defined benefit plan and contribution plan. The employee pension benefit is managed at the OUSD level. The measurement of the service cost requires the use of an actuarial cost method and assumptions. The OPM administers these benefits and provides the factors that DLA GF applies to calculate and recognize imputed costs, as reported in its Statements of Net Cost, and a corresponding imputed revenue in the Statements of Changes in Net Position. DLA GF is not responsible for and does not report CSRS or FERS assets, accumulated plan benefits, or liabilities applicable to its employees. OPM is responsible for and reports these amounts.

## R. Net Position

Net position is the residual difference between assets and liabilities and consists of unexpended appropriations and cumulative results of operations.

**Unexpended Appropriations:** Unexpended appropriations consist of unobligated and undelivered order balances. Unobligated balances are amounts of budgetary resources available for obligation, which have not been rescinded or withdrawn. Undelivered orders are the amount of obligations incurred for goods and/or services ordered, but not yet received. DLA GF unexpended appropriations primarily consist of direct appropriations.

**Cumulative Results of Operations:** Cumulative results of operations includes the net difference since inception between: (1) expenses and losses; (2) revenue, gains; and (3) other financing sources.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Revenue, and Unfilled Customer Orders and Accounts Payable, Expenses, and Undelivered Orders, Note 11, *Statement of Budgetary Resources*; and Note 13, *Restatement*.)

## S. Revenue and Other Financing Sources

**Exchange and Non-exchange Revenue:** The DLA GF classifies revenue as either exchange revenue or non-exchange revenue. Exchange revenue arises when DLA GF provides goods or services to intragovernmental or Other than Intragovernmental entities in exchange for inflows of resources. Exchange revenue is presented in the Statements of Net Cost and serves to offset the costs of these goods and services. Exchange revenue from services in the O&M appropriation include support for Continuity of Operations; Law Enforcement Support Office; Morale, Welfare and Recreation; and Defense Travel System Support. Exchange revenue from services in the RDT&E appropriation include support for the Next Generation Resource Management System; Mapping EBS; and Defense Information System Security.

Non-exchange revenue is derived from the government's sovereign right to demand payment, such as specifically identifiable, legally enforceable claims. Non-exchange revenue is considered to impact the cost of DLA GF's operations and is reported in the Statements of Changes in Net Position as a financing source.

**Other Financing Sources:** Other financing sources, other than exchange and non-exchange revenue, include additional inflows of resources that increase results of operations during the reporting period. DLA GF's other financing sources come from unexpended appropriation transfers and non-expenditure transfers-in initiated by OUSD and recognized as financing sources when used. Other financing sources also include: (1) transfers-in/out without reimbursement, and (2) imputed financing with respect to costs subsidized by another Federal entity.

Transfers-in/out without Reimbursement: Transfers-in/out without reimbursement include intragovernmental transfers of capitalized assets. The amount of the transfer is the book value of the transferring entity and if the book value is not known, the amount should be the estimated fair value at the date of transfer.

Imputed Financing and Imputed Cost: In certain cases, DLA GF receives goods and services from other Federal entities at no cost or at a cost less than the full cost to the providing entity. Consistent with accounting standards, certain costs of the providing entity that are not fully reimbursed by DLA GF are recognized as imputed cost in the Statements of Net Cost and are offset by imputed financing in the Statements of Changes in Net Position. DLA GF recognizes the following imputed cost and related imputed financing: (1) employee benefits administered by the OPM (i.e., retirement, health, life insurance benefits); and (2) claims settled by the Treasury Judgment Fund. In accordance with SFFAS 55, *Amending Inter-Entity Costs Provisions*, unreimbursed costs of goods and services other than those identified above are not included in DLA GF financial statements.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Revenue, and Unfilled Customer Orders).

## T. Expenses

Expenses are recognized when there are outflows, usage of assets, or incurrences of liabilities (or a combination) from carrying out activities related to DLA GF appropriations and missions, for which benefits do not extend beyond the present operating period. For financial reporting purposes, operating expenses are recognized in the period incurred (refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders, and Note 13, *Restatement*).

**Apache Check**

Army Cpl. Daisy Chikwanha, an AH-64 helicopter repairer assigned to the 1st Battalion, 3rd Aviation Regiment, 12th Combat Aviation Brigade, inspects an Apache helicopter during Exercise Swift Response 23 at the Stefanovikeio Airport in Greece, May 9, 2023. **Photo By:** Army Sgt. Maria Henderson

# Note 2: Fund Balance with Treasury (Unaudited)

Fund Balance with Treasury as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Status of Fund Balance Treasury** | | |
| Unobligated Balance: | | |
| Available | $ 497,218 | $ 567,259 |
| Unavailable | 84,068 | 43,261 |
| Obligated Balance not yet Disbursed | 1,670,028 | 1,796,143 |
| **Total Fund Balance with Treasury** | **$ 2,251,314** | **$ 2,406,663** |

**Status of Fund Balance with Treasury** presents the budgetary and proprietary balances that constitute DLA GF FBwT. It consists of unobligated and obligated balances. The balances reflect the budgetary authority remaining for disbursement against current or future obligations. Unobligated and obligated balances differ from the related amounts reported in the Combined Statements of Budgetary Resources because budgetary balances are supported by amounts other than FBwT (e.g., budgetary receivables).

**Unobligated Balance – Available** includes the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations and can be used for future obligations.

**Unobligated Balance – Unavailable** includes the cumulative amount of budget authority and funds not available for obligation from offsetting collections.

**Obligated Balance Not Yet Disbursed** includes funds that have been obligated for goods and services not received, as well as those received but not paid.

**Non-budgetary FBwT** consists of FBwT in unavailable receipt accounts and clearing accounts that do not have budget authority and non-budgetary FBwT such as non-fiduciary deposit funds. As of September 30, 2023 and 2022, DLA GF does not have balances for non-budgetary FBwT.

**Other Information** includes the following tables summarizing the undistributed collections and disbursements between U.S. Treasury and DLA GF as of September 30, 2023 and 2022, respectively.

**FY 2023 Adjustments of Undistributed Collections and Disbursements (dollars in thousands)**

| Transaction Type | Treasury Balance based on CMR | DLA GF Trial Balance | Balances Not Yet Recorded in DLA Accounting System - Undistributed |
|---|---|---|---|
| Collections | $ 417,865 | $ 422,987 | $ (5,122) |
| Disbursements | $ 4,800,116 | $ 4,386,808 | $ 413,308 |

**FY 2022 Adjustments of Undistributed Collections and Disbursements (dollars in thousands)**

| Transaction Type | Treasury Balance based on CMR | DLA GF Trial Balance | Balances Not Yet Recorded in DLA Accounting System - Undistributed |
|---|---|---|---|
| Collections | $ 370,111 | $ 376,662 | $ (6,551) |
| Disbursements | $ 3,663,688 | $ 3,246,180 | $ 417,508 |

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Fund Balance with Treasury.)

# Note 3: Accounts Receivable, Net (Unaudited)

Accounts Receivable, Net as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | Accounts Receivable | (Less: Allowance for Doubtful Accounts) | Accounts Receivable, Net |
|---|---|---|---|
| **Intragovernmental Accounts Receivable, Net** | | | |
| Operations and Maintenance | $ 6,610 | $ - | $ 6,610 |
| Research, Development, Test & Evaluation | 8,158 | - | 8,158 |
| **Total Intragovernmental Accounts Receivable, Net** | **$ 14,768** | **-** | **$ 14,768** |
| **Other than Intragovernmental Accounts Receivable** | | | |
| Operations and Maintenance | 29 | - | 29 |
| **Total Other than Intragovernmental Accounts Receivable** | **29** | **-** | **29** |
| **Total Accounts Receivable** | **$ 14,797** | **$ -** | **$ 14,797** |

| FY 2022 | Accounts Receivable | (Less: Allowance for Doubtful Accounts) | Accounts Receivable, Net |
|---|---|---|---|
| **Intragovernmental Accounts Receivable, Net** | | | |
| Operations and Maintenance | $ 4,420 | $ (45) | $ 4,375 |
| Research, Development, Test & Evaluation | 9,404 | - | 9,404 |
| **Total Intragovernmental Accounts Receivable, Net** | **$ 13,824** | **$ (45)** | **$ 13,779** |
| **Other than Intragovernmental Accounts Receivable** | | | |
| Operations and Maintenance | $ 14 | $ - | $ 14 |
| Research, Development, Test & Evaluation | 1 | - | 1 |
| **Total Other than Intragovernmental Accounts Receivable** | **$ 15** | **$ -** | **$ 15** |
| **Total Accounts Receivable** | **$ 13,839** | **$ (45)** | **$ 13,794** |

In FY 2022, DLA GF implemented Technical Bulletin 2020-1, *Loss Allowance for Intragovernmental Receivables*, and recognized an allowance for doubtful accounts for its intragovernmental accounts receivable. As of September 30, 2023 and 2022, DLA GF reported $0 and $45.4 thousand respectively in intragovernmental allowance for doubtful accounts.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Revenue, and Unfilled Customer Orders.)

# Note 4: Inventory and Related Property, Net (Unaudited)

Inventory and Related Property, Net as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | Valuation Method | FY 2023 | FY 2022 |
|---|---|---|---|
| **Inventory Categories:** | | | |
| Held for Sale | MAC | $ - | $ 12,052 |
| Inventory Work-In-Process | MAC | $ - | 17,434 |
| **Total Inventory and Related Property, Net** | | **$ -** | **$ 29,486** |

**MAC** = Moving Average Cost

The DLA GF inventory is comprised of military equipment in the Military GPS User Equipment ASIC Program. It is DLA's mission to procure, receipt, store and issue the material as required, and recognize the material as inventory held for sale upon receipt. These assets are transferred to the DLA WCF SCM - DLA Land & Maritime.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Inter-Entity Cost and Inventory and Related Property, Net.)

# Note 5: General Property, Plant and Equipment (Unaudited)

General Property, Plant and Equipment as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | | | |
|---|---|---|---|
| | Acquisition Value | Accumulated Depreciation/ Amortization | Net Book Value |
| **Major Asset Classes** | | | |
| General Equipment | $ 435 | $ (174) | $ 261 |
| Construction-in-Progress | 497,520 | - | 497,520 |
| Internal-Use Software | 8,647 | (721) | 7,926 |
| Internal-Use Software in Development | 21,151 | - | 21,151 |
| **Total General Property, Plant and Equipment, Net** | **$ 527,753** | **$ (895)** | **$ 526,858** |

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| FY 2022 Restated | | | |
|---|---|---|---|
| | Acquisition Value | Accumulated Depreciation/ Amortization | Net Book Value |
| **Major Asset Classes** | | | |
| General Equipment | $ 435 | $ (49) | $ 386 |
| Construction-in-Progress | 370,720 | - | 370,720 |
| Internal-Use Software | - | - | - |
| Internal-Use Software in Development | 21,145 | - | 21,145 |
| **Total General Property, Plant and Equipment, Net** | **$ 392,300** | **$ (49)** | **$ 392,251** |

The DLA GF maintains CIP, IUS, and IUS in Development, and General Equipment. The CIP mainly consists of projects from USACE and NAVFAC. The accumulated CIP balances will be transferred to WCF upon completion of the project and removed from DLA GF accounting records. As of September 30, 2023, DLA GF continues to review the CIP balance reported by the construction agents to DFAS and adjustments are made as applicable by DLA GF and DFAS.

The Internal-Use Software mainly consists of DAI Oracle Software Perpetual Licenses. The Internal-Use Software in Development mainly consists of projects related to DAI systems.

General Equipment consists of equipment managed by DMEA.

The table below discloses activity for General Property, Plant and Equipment as of September 30, 2023, and 2022, respectively (dollars in thousands):

| | FY 2023 | FY 2022 Restated |
|---|---|---|
| **General Property, Plant and Equipment - Beginning Balances** | **$ 392,251** | **$ 604,790** |
| Correction of Errors | **-** | **(50,127)** |
| **Beginning Balances, As Adjusted** | **392,251** | **554,663** |
| Capitalized Acquisitions | 200,127 | 195,661 |
| Depreciation Expense | (846) | (49) |
| Dispositions | (385) | **-** |
| Transfers in/out without reimbursements | (64,289) | (358,024) |
| **General Property, Plant and Equipment - Ending Balances** | **$ 526,858** | **$392,251** |

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to General Property, Plant and Equipment, Net, and Leases.)

# Note 6: Liabilities Not Covered by Budgetary Resources (Unaudited)

Liabilities not Covered by Budgetary Resources as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 Restated |
|---|---|---|
| **Intragovernmental Liabilities** | | |
| Other Current Liabilities - Benefits Program Contributions Payable | $ 1,324 | $ 913 |
| **Total Intragovernmental Liabilities** | **1,324** | **913** |
| | | |
| **Other than Intragovernmental Liabilities** | | |
| Accounts Payable | 7,324 | 7,758 |
| Environmental and Disposal Liabilities | 67,924 | 68,683 |
| Federal Employee Benefits Payable | 8,546 | 7,496 |
| **Total Other than Intragovernmental Liabilities** | **83,794** | **83,937** |
| **Total Liabilities Not Covered by Budgetary Resources** | **85,118** | **84,850** |
| **Total Liabilities Covered by Budgetary Resources** | **79,145** | **84,055** |
| **Total Liabilities** | **$ 164,263** | **$ 168,905** |

**Other Current Liabilities – Benefits Program Contributions Payable (Intragovernmental)** primarily consist of intragovernmental liabilities for unemployment compensation and the accrued FECA liability based on DOL records.

**Accounts Payable (Other than Intragovernmental)** include amounts owed but not yet paid to the public for goods and services received by DLA GF. It is classified as Liabilities Not Covered by Budgetary Resources because the revenues or other sources of funds necessary to pay the liabilities have not been made available through congressional appropriations or current earnings of DLA.

**Environmental and Disposal Liabilities (Other than Intragovernmental)** consist of probable and reasonably estimable future outflow or expenditure of resources that exist as of the financial reporting date for environmental cleanup costs resulting from past transactions or events. As of September 30, 2023 and 2022, the total liabilities covered by budgetary resources for the E&DL consists of $8.5 million and $9.7 million, respectively.

**Federal Employee Benefits Payable (Other than Intragovernmental)** are primarily comprised of the current year: (1) FECA actuarial liability based on DOL records and (2) unfunded annual leave earned by civilian employees but not yet paid. Unfunded annual leave includes restored leave, compensatory time, and credit hours as earned.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders; Note 7, *Federal Employee Benefits Payable and Related Other Liabilities*; and Note 8, *Environmental and Disposal Liabilities*.)

# Note 7: Federal Employee Benefits Payable and Related Other Liabilities (Unaudited)

Federal Employment Benefits Payable and Related Other Liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | Liabilities | (Less: Assets Available to Pay Benefits) | Unfunded Liabilities |
|---|---|---|---|
| **Intragovernmental Other Liabilities** | | | |
| Employer Contribution and Payroll Taxes Payable | $ 422 | $ (422) | $ - |
| Unfunded FECA Liability | 288 | - | 288 |
| Other Unfunded Employment Related Liability | 1,036 | - | 1,036 |
| **Total Intragovernmental Other Liabilities** | $ 1,746 | $ (422) | $ 1,324 |
| **Other than Intragovernmental Federal Employee Benefits Payable** | | | |
| Actuarial FECA Liability | $ 2,738 | $ - | $ 2,738 |
| Accrued Unfunded Annual Leave | 5,808 | - | 5,808 |
| Employer Contributions and Payroll Taxes Payable | 609 | (609) | - |
| **Total Other than Intragovernmental Federal Employee Benefits Payable** | **$ 9,155** | **$ (609)** | **$ 8,546** |

| FY 2022 | Liabilities | (Less: Assets Available to Pay Benefits) | Unfunded Liabilities |
|---|---|---|---|
| **Intragovernmental Other Liabilities** | | | |
| Employer Contribution and Payroll Taxes Payable | $ 393 | $ (393) | $ - |
| Unfunded FECA Liability | 290 | - | 290 |
| Other Unfunded Employment Related Liability | 623 | - | 623 |
| **Total Intragovernmental Other Liabilities** | **$ 1,306** | **$ (393)** | **$ 913** |
| **Other than Intragovernmental Federal Employee Benefits Payable** | | | |
| Actuarial FECA Liability | $ 2,137 | $ - | $ 2,137 |
| Accrued Unfunded Annual Leave | 5,359 | - | 5,359 |
| Employer Contributions and Payroll Taxes Payable | 545 | (545) | - |
| **Total Other than Intragovernmental Federal Employee Benefits Payable** | **$ 8,041** | **$ (545)** | **$ 7,496** |

**Employer Contributions and Payroll Taxes Payable (Intragovernmental)** are the employer portion of payroll taxes and benefit contributions for health benefits, retirement, life insurance and voluntary separation incentive payments.

**Unfunded FECA Liability (Intragovernmental)** include the accrued FECA liability paid by DOL but not yet reimbursed by DLA GF.

**Other Unfunded Employment Related Liability (Intragovernmental)** consist of intragovernmental liabilities for unemployment compensation.

**Actuarial FECA Liability (Other than Intragovernmental)** are workers' compensation benefits developed by the DOL's Office of Worker's Compensation Programs (OWCP) and provided to DLA GF at the end of each FY. 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 OMB economic assumptions for 10-year U.S. Treasury notes and bonds. COLAs and medical inflation factors are also applied to the calculation of projected future benefits.

**Accrued Unfunded Annual Leave (Other than Intragovernmental)** includes restored leave, compensatory time, and credit hours earned.

(Refer to Note 6, *Liabilities Not Covered by Budgetary Resources*.)

**National Guard Medical Readiness**

Pete Ramos, logistics management specialist at Army Medical Logistics Command, addresses other members of his working group during a workshop on Medical Logistics in Campaigning and its impact on the National Guard and Reserve at Joint Base San Antonio-Fort Sam Houston Nov. 29, 2022. **Photo By:** Kathryn Ellis-Warfield

# Note 8: Environmental and Disposal Liabilities (Unaudited)

Environmental and Disposal Liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 Restated |
|---|---|---|
| Environmental and Disposal Liabilities | | |
| Accrued Environmental Restoration Liabilities: | | |
| Active Installations - Installation Restoration Program and Building Demolition and Debris Removal | $ 76,446 | $ 78,346 |
| **Total Environmental and Disposal Liabilities** | **$ 76,446** | **$ 78,346** |

The DLA GF E&DL are comprised of two primary elements: (1) existing obligations supporting the Defense Environmental Restoration Account (DERA) and BRAC funded environmental restoration programs, and (2) the CTC which includes anticipated future cost necessary to complete environmental restoration sites. While DLA GF is responsible for recording BRAC Installations – Installation Restoration Program (IRP) E&DL, associated costs are reported on the DoD Component Level Statements under Consolidated ODO GF.

In FY 2023 and FY 2022, DLA GF utilized the RACER software to generate the CTC estimates of anticipated future costs.

As of September 30, 2023, and 2022, the total GF E&DL consist of $76.4 million and $78.3 million, respectively.

In FY 2023 cost estimates under the Defense Environmental Restoration Program (DERP) were generated for sites with Accrued Environmental Restoration Liabilities Active Installations – IRP E&DL and BRAC Installations – IRP E&DL. While DLA GF is responsible for recording BRAC Installations –IRP E&DL, associated costs are reported on the DoD Component Level Statements under Consolidated ODO GF.

**Types of Environmental and Disposal Liabilities:** The DLA GF is responsible for cleanup requirements of DERP eligible sites managed under Active IRP and BRAC IRP. Costs under the Accrued Environmental Restoration Liabilities and BRAC Installations line items represent the cost to correct past environmental problems that are funded from the Environmental Restoration and BRAC Accounts in accordance with the DoD Manual (DoDM) 4715.20 – *DERP Management* (March 2012) and the DoD 7000.14-R Financial Management Regulation (FMR) Volume 4, Chapter 13 – *Environmental and Disposal Liabilities* (March 2022). All clean-up is conducted in coordination with regulatory agencies, other responsible parties, and current property owners.

The DLA GF reportable E&DL is under Accrued Environmental Restoration Liabilities and BRAC Installations and includes the following line items:

Accrued Environmental Restoration Liabilities: Includes Active Installations – IRP E&DL associated with remedial actions eligible for funding under the DERP. These remedial actions may address hazardous substances, pollutants, and contaminants as defined in the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA); hazardous waste or hazardous constituents addressed under the RCRA corrective action process or other Federal or state statutes and regulations; and military munitions or Waste Military Munitions, chemical residues from military munitions, and munitions scrap at locations other than operational ranges associated with an active installation, when the environmental restoration activity is incidental to the IRP environmental restoration activity.

BRAC Installations: Includes IRP E&DL associated with the costs to address environmental cleanup at bases that are realigning or closing resulting from past activities which are part of DERP. While DLA GF is responsible for recording BRAC Installations – IRP E&DL, it is reported in the DoD Component Level Statements under Consolidated ODO GFs.

The DLA assessed its PP&E inventory and does not currently have reportable GF E&DL for Environmental Closure, Asbestos, or General Equipment. There are no other reportable E&DL

categories as listed on the DoD FMR Volume 6B, Chapter 10 – *Notes to the Financial Statements*, *Chapter 10, Paragraph 17 Environmental and Disposal Liabilities* (February 2023).

**Applicable Laws and Regulations for Cleanup Requirements:** The DLA GF 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. DLA GF is required to comply with the following laws and regulations where applicable: CERCLA; the Superfund Amendments and Reauthorization Act; RCRA; and other applicable Federal, State, and local laws and regulations. Required cleanup may at times extend beyond Installation boundaries onto privately owned property or onto sites where DLA GF is named as a potentially responsible party by a regulatory agency. DLA GF reports E&DL in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*, and Federal Financial Accounting Technical Release 2, *Determining Probable and Reasonably Estimable for Environmental Liabilities in the Federal Government*.

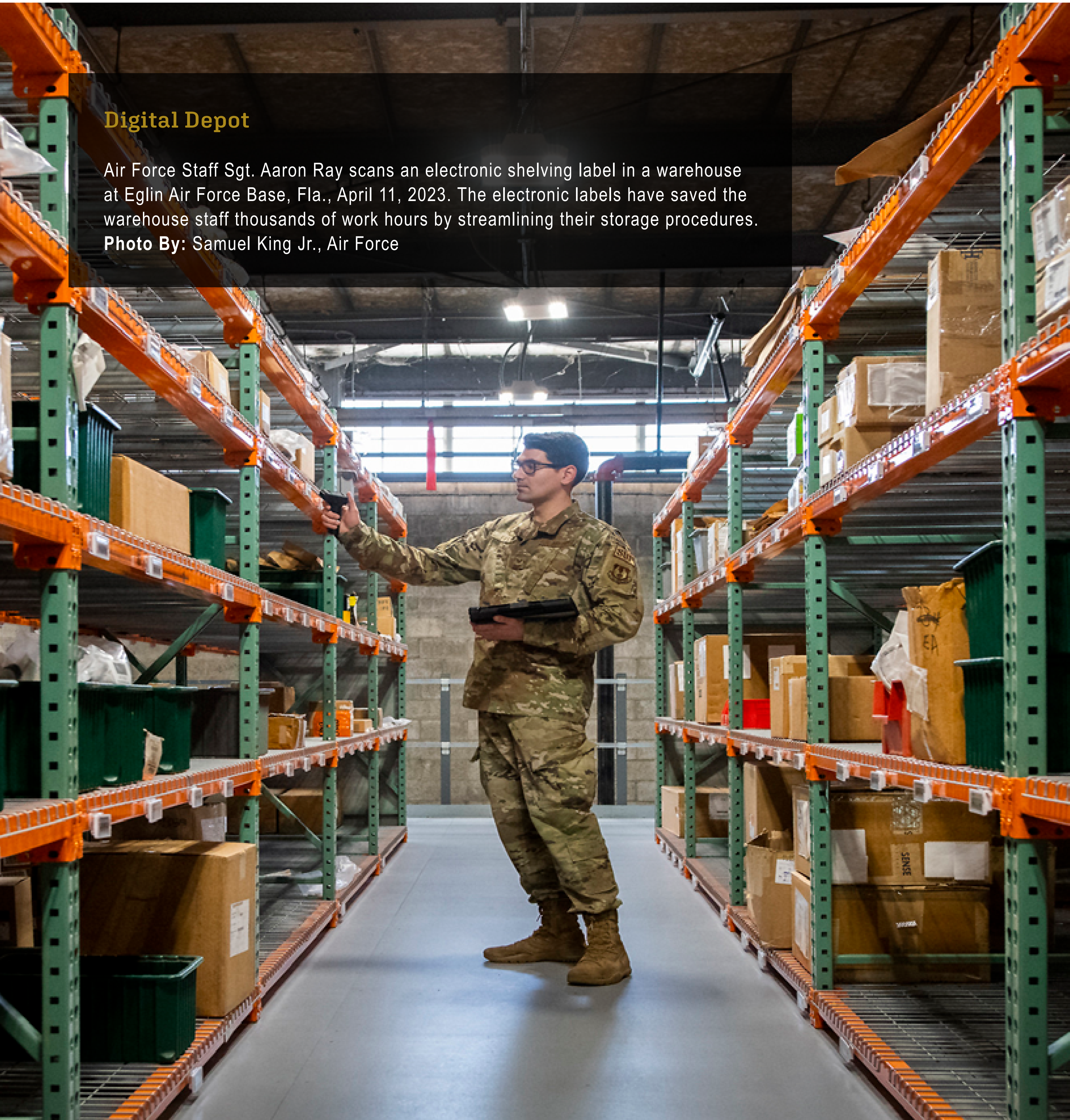
**Methods for Assigning Estimated Total Cleanup Costs to Current Operating Periods:**
To estimate future environmental costs, DLA GF utilizes a combination of historical or pre-negotiated contract costs, proposal costs, engineering estimates, and in the absence of other detailed information, parametric estimates created using the RACER software. Any historical costs used in the creation of the estimates for DLA E&DL are adjusted for inflation and reported in current year dollars. The RACER Steering Committee ensures that the RACER software is VV&A in accordance with DoD Instruction 5000.61 DoD M&S Verification, Validation, and Accreditation. The DoD is working with the RACER Steering Committee and stakeholders to identify improvements to RACER functionality, auditability, and documentation. Detailed information on estimating methodologies is provided in the DLA ELM SOPs.

**Nature of Estimates and the Disclosure of Information Regarding Possible Changes Due to Inflation, Deflation, Technology, or Applicable Laws and Regulations:** The DLA E&DL Site ID process tracks environmental events such as spills and releases in an Environmental Event Repository and evaluates each event annually for E&DL potentiality to determine the annual CTC inventory. The DLA GF E&DL estimates are created annually for all projected requirements and are finalized and approved by July. The estimates are then reevaluated through a roll forward review to identify any material changes to previously approved estimates to ensure accuracy as of the financial reporting date of September 30. Processes are conducted in accordance with DLA ELM SOPs; DoDM 4715.20 – *DERP Management* (March 2012) and the DoD 7000.14-R FMR Volume 4, Chapter 13 – E*nvironmental and Disposal Liabilities* (March 2022).

CTC estimates revised through roll forward, as applicable, and prior year obligations are reported in the balance as of September 30. As of the reporting date, no material changes in the total estimated cleanup costs were identified through the roll forward review due to changes in laws, technology, or plans. In addition, DLA is not aware of any changes to GF E&DL estimates that would result from inflation, deflation, technology, plans, and or pending changes to applicable laws and regulation. The cost estimate changes from prior periods are primarily driven by remediation activities and operations, as evidenced by UDOs; there are minor adjustments for inflation or other similar administrative costs throughout the fiscal year. E&DL estimates will be reevaluated each year and may change in the future due to changes in laws and regulations, changes in agreements with regulatory agencies, and advances in technology.

**Uncertainty Regarding the Accounting Estimates Used to Calculate the Reported Environmental and Disposal Liabilities:** The stated total DLA GF E&DL includes prior year obligations and the estimate of future costs necessary to complete requirements. DLA GF has instituted extensive controls to ensure that these estimates are accurate and reproducible. The cost estimates produced through the E&DL process are considered accounting estimates, which require certain judgments and assumptions that are reasonable based upon information available at the time the estimates are calculated. Actual cost may materially vary from the accounting estimates if agreements with regulatory agencies require remediation to a different degree than anticipated when calculating the estimates. DLA GF E&DL can be further affected if investigation of the environmental sites reveals contamination levels that differ from the estimated parameters.

The DLA utilizes a formalized Site ID process to identify, track, and evaluate environmental events where the potential for an out-year E&DL exists but the E&DL is not probable and measurable. These environmental events are tracked and will be re-evaluated in the following fiscal year to determine if any changes have taken place and sufficient information, or data is available to create an estimate of future costs that would be included in the GF E&DL balance. (Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities and Commitments and Contingencies.)



## Digital Depot

Air Force Staff Sgt. Aaron Ray scans an electronic shelving label in a warehouse at Eglin Air Force Base, Fla., April 11, 2023. The electronic labels have saved the warehouse staff thousands of work hours by streamlining their storage procedures. **Photo By:** Samuel King Jr., Air Force

# Note 9: Other Liabilities (Unaudited)

Other Liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | Current | Non-Current | Total |
|---|---|---|---|
| **Other than Intragovernmental Other Liabilities** | | | |
| Accrued Funded Payroll and Benefits | $ 1,978 | $ - | $ 1,978 |
| Contract Holdbacks | 1,839 | - | 1,839 |
| **Total Other than Intragovernmental Other Liabilities** | **$ 3,817** | **$ -** | **$ 3,817** |

| FY 2022 | Current | Non-Current | Total |
|---|---|---|---|
| **Other than Intragovernmental Other Liabilities** | | | |
| Accrued Funded Payroll and Benefits | $ 1,757 | $ - | $ 1,757 |
| Contract Holdbacks | 1,345 | - | 1,345 |
| **Total Other than Intragovernmental Other Liabilities** | **$ 3,102** | **$ -** | **$ 3,102** |

**Accrued Funded Payroll and Benefits (Other than Intragovernmental)** include salaries, wages, and other compensation earned by employees but not yet disbursed.

**Contract Holdbacks (Other than Intragovernmental)** are amounts earned by contractors or suppliers during the production period but not yet paid to the contractor/supplier to ensure future performance.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders.)

**Domestic Germanium Recycling Capability**

Hawaii Air National Guard Senior Airman Samson Aina, a C-17 loadmaster assigned to the 204th Airlift Squadron, adjusts night vision goggles aboard a C-17 Globemaster III aircraft at Joint Base Pearl Harbor-Hickam, Hawaii. A Defense Logistics Agency recycling program allows optical-grade germanium to be reused in new equipment and is used often in night vision technologies. **Photo By:** Air Force Master Sgt. Mysti Bicoy, Hawaii Air National Guard

# Note 10: Commitments and Contingencies (Unaudited)

Accrued and reasonably possible environmental contingent liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | | | | |
|---|---|---|---|---|
| | Accrued Liabilities | Estimated Range of Loss | | |
| | | Lower End | Upper End | |
| **Environmental Contingencies** | | | | |
| Probable | $ 76,466 | $ - | - | |
| Reasonably Possible | $ - | $ - | - | |

| FY 2022 Restated | | | |
|---|---|---|---|
| | Accrued Liabilities | Estimated Range of Loss | |
| | | Lower End | Upper End |
| **Environmental Contingencies** | | | |
| Probable | $ 78,346 | $ - | $ - |
| Reasonably Possible | $ - | $ - | $ - |

**Environmental Contingencies:** The DLA GF has developed a process to identify, estimate, and record contingent E&DL. DLA GF does not estimate a potential range of loss in this process. Where DLA GF is aware of probable and measurable future outflow of resources due to a past event or exchange transaction, the appropriate program categories are reported in Note 8, *Environmental and Disposal Liabilities*.

**Legal Contingencies:** The DLA GF was not a party in administrative proceedings or legal actions as of September 30, 2023 and 2022. DLA's EWSC is used by the Office of General Counsel to report the outcomes and possible liability amounts of open cases.

Cases for which legal counsel determines an adverse outcome is reasonably possible and the possible financial outflow is measurable, are not recorded, but disclosed as reasonably possible for financial reporting purposes.

As of September 30, 2023, DLA does not have any matters that are identified as a probable or reasonably possible liability, and zero matters that are identified as remote liabilities.

**Commitments:** The DLA GF does not have obligations related to canceled appropriations for contractual commitments.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities and Commitments and Contingencies; Note 5, *Liabilities Not Covered by Budgetary Resources*; and Note 8, *Environmental and Disposal Liabilities*.)

# Note 11: Statement of Budgetary Resources (Unaudited)

**Unobligated Balance Brought Forward, October 1:** There were no adjustments during the current year to correct the unobligated balance brought forward, October 1. Components of the amount reported as "Unobligated Balance from Prior Year Budget Authority, net" are disclosed in the table below. Other adjustments consist of recoveries of prior year obligated balances and unobligated balances transferred from other accounts. The following table displays a reconciliation between the prior year's unobligated balance, end of year amount to the current year's unobligated balance from prior year budget authority, net amount (dollars in thousands).

| | FY 2023 | FY 2022 |
|---|---|---|
| **Reconciliation of PY Ending Unobligated Balances of CY Beginning Unobligated Balances** | | |
| Unobligated balance brought forward, October 1 | $ 610,519 | $ 615,991 |
| Unobligated balance transferred to other accounts (-) | (160) | - |
| Unobligated balance transferred from other accounts | 2,450 | 6,150 |
| Unobligated balance transferred between expired and unexpired accounts (+ or -) | 80 | (10,212) |
| Recoveries of prior year unpaid obligations | 73,442 | 30,073 |
| Other balances withdrawn (-) | (18,940) | (30,307) |
| Recoveries of prior year paid obligations | 428 | 5 |
| **Unobligated Balance, Total** | **$ 667,819** | **$ 611,700** |

**Undelivered Orders (UDOs):** for the years ended September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Intragovernmental Undelivered Orders** | | |
| Unpaid | $ 482,830 | $ 572,679 |
| **Total Intragovernmental Undelivered Orders** | **482,830** | **572,679** |
| **Other than Intragovernmental Undelivered Orders** | | |
| Unpaid | 1,184,561 | 1,201,952 |
| Paid | 113,922 | 7,741 |
| **Total Other than Intragovernmental Undelivered Orders** | **1,298,483** | **1,209,693** |
| **Total Undelivered Orders** | **$ 1,781,313** | **$ 1,782,372** |

UDOs represent the amount of goods and/or services ordered to perform DLA GF's mission objectives that have not been received. Unpaid UDOs represent obligations for goods and services that have not been received or paid. Whereas paid UDOs represent obligations for goods and services that have been paid for in advance of receipt. For the years ended September 30, 2023, and 2022, respectively, DLA GF does not have intragovernmental paid UDO balances.

Due to system limitations, DLA GF is unable to determine the Intragovernmental and Other than Intragovernmental allocation of UDOs. DLA GF estimates the allocation of Intragovernmental and Other than Intragovernmental unpaid UDOs based on funded liabilities, excluding payroll and employee benefit liabilities, and paid UDOs based on advances and prepayments reported on the Balance Sheets.

(Refer to Note 1.C., Departures from U.S. GAAP, related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions, and Accounts Payable, Expenses, and Undelivered Orders.)

# Note 12: Reconciliation of Net Cost to Net Outlays (Unaudited)

Reconciliation of Net Cost to Net Outlays for the years ended September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | | | |
|---|---|---|---|
| | Intragovernmental | Other than Intragovernmental | Total |
| **NET COST** | **$ 165,896** | **$ 601,106** | **$ 767,002** |
| **Components of Net Cost That are Not Part of Net Outlays** | | | |
| General Property, Plant, and Equipment Depreciation | - | (846) | (846) |
| General PP&E Disposals | - | (385) | (385) |
| **Increase/(Decrease) in Assets** | | | |
| Accounts Receivable, Net | 989 | 14 | 1,003 |
| Advances and Prepayments | - | 106,181 | 106,181 |
| **(Increase)/Decrease in Liabilities** | | | |
| Accounts Payable | 2,156 | 2,854 | 5,010 |
| Environmental and Disposal Liabilities | - | 1,900 | 1,900 |
| Federal Employee Benefits Payable | - | (1,114) | (1,114) |
| Advances from Others and Deferred Revenue | - | 1 | 1 |
| Other Liabilities | (441) | (715) | (1,156) |
| **Other Financing Sources** | | | |
| Imputed Financing | (4,546) | - | (4,546) |
| **Total Components of Net Cost That are Not Part of Net Outlays** | **(1,842)** | **107,890** | **106,048** |
| **Components of Net Outlays That are Not Part of Net Cost** | | | |
| Acquisition of PP&E | - | 200,127 | 200,127 |
| Acquisition of Inventory and Related Property | - | 86,925 | 86,925 |
| **Financing Sources:** | | | |
| Transfers out (in) without reimbursements | - | - | - |
| **Total Components of Net Outlays That are Not Part of Net Cost** | **-** | **287,052** | **287,052** |
| **NET OUTLAYS** | **$ 164,054** | **$ 996,048** | **1,160,102** |
| **Outlays, Net, Statements of Budgetary Resources** | | | **1,160,102** |
| **Reconciling Difference** | | | **$ -** |

| FY 2022 Restated | Intragovernmental | Other than Intragovernmental | Total |
|---|---|---|---|
| **NET COST** | **$ 187,967** | **$ 520,786** | **$ 708,753** |
| **Components of Net Cost That are Not Part of Net Outlays** | | | |
| General Property, Plant, and Equipment Depreciation | - | (49) | (49) |
| General PP&E Disposals | - | - | - |
| **Increase/(Decrease) in Assets** | | | |
| Accounts Receivable, Net | 225 | (5) | 220 |
| Advances and Prepayments | - | 7,741 | 7,741 |
| **(Increase)/Decrease in Liabilities** | | | |
| Accounts Payable | 12,122 | (41,284) | (29,162) |
| Environmental and Disposal Liabilities | - | 12,201 | 12,201 |
| Federal Employee Benefits Payable | - | 976 | 976 |
| Advances from Others and Deferred Revenue | - | 853 | 853 |
| Other Liabilities | 5,122 | 631 | 5,753 |
| **Other Financing Sources** | | | |
| Imputed Financing | (2,789) | - | (2,789) |
| **Total Components of Net Cost That are Not Part of Net Outlays** | **14,680** | **(18,936)** | **(4,256)** |
| **Components of Net Outlays That are Not Part of Net Cost** | | | |
| Acquisition of PP&E | - | 195,661 | 195,661 |
| Acquisition of Inventory and Related Property | - | 12,052 | 12,052 |
| **Financing Sources:** | | | |
| Transfers out (in) without reimbursements | (6) | - | (6) |
| **Total Components of Net Outlays That are Not Part of Net Cost** | **(6)** | **207,713** | **207,707** |
| **NET OUTLAYS** | **$ 202,641** | **$ 709,563** | **912,204** |
| **Outlays, Net, Statements of Budgetary Resources** | | | **912,204** |
| **Reconciling Difference** | | | **$ -** |

The Net Cost to Net Outlays Reconciliation schedule reconciles the Net Cost (reported in the Statements of Net Cost) to the Net Outlays (reported in the Statements of Budgetary Resources). The reconciliation clarifies the relationship between budgetary and proprietary accounting information. Examples of the reconciling items identified are: (1) Transactions which did not result in an outlay but did result in a cost; and (2) Unpaid expenses included in the net cost in this reporting period but not yet included in outlays. Components of net cost that are not part of net outlays are most commonly: (1) the result of allocating assets to expenses over more than one reporting period (e.g., depreciation) and the write-down of assets (due to revaluations); (2) the temporary timing differences between outlays/receipts and the operating expense/revenue during the period; and (3) costs financed by other entities (imputed inter-entity cost).

For FY 2023, the key reconciling differences between the net cost and net outlays for DLA GF include: (1) Advances and Prepayments related to commercial interim financing payments for PDW and (2) the acquisition of capital assets that have no impact on net cost.

For FY 2022, the key reconciling differences between the net cost and net outlays for DLA GF include: (1) Accounts Payable increased due to a judgement fund liability for a contract dispute related to the MILCON program; (2) Advances and Prepayments related to commercial interim financing payments for DMEA microchips; (3) the acquisition of capital assets, which are capitalized expenditures paid for, that have no impact on net cost.

Any reconciling difference would be attributable to limitations of financial and nonfinancial management processes and systems that support the financial statements, as disclosed in Note 1.B., *Basis of Presentation and Accounting*. In addition, DLA GF does not have an established policy to identify and reconcile net cost to net outlays and/or identify components of net cost or net outlays that have not been properly accounted for. As such, DLA GF will continue to investigate and resolve the causes of any reconciling differences.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Revenue, and Gains, Inventory and Related Property, Net, General Property, Plant and Equipment, Net, Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions, Accounts Payable, Undelivered Orders, and the Reconciliation of Net Cost to Net Outlays.)

**Link Labor**

Navy Seamen Kevoy Gordon, left, and Andrew Crickard sand and prepare the USS Tripoli's anchor chain for painting during a maintenance availability in San Diego, April 20, 2023. **Photo By:** Navy Petty Officer 1st Class Danian C. Douglas

**Artic Gold**

Airmen set up a tent during Arctic Gold at Eielson Air Force Base, Alaska, April 14, 2023. During the exercise, airmen trained to provide support in an expeditionary deployed environment. **Photo By:** Air Force Airman 1st Class Ricardo Sandoval

# Note 13: Restatement (Unaudited)

In FY 2023, DLA GF restated its FY 2022 financial statements to correct errors in the Balance Sheet, Statement of Net Cost, and Statement of Changes in Net Position. The impact of these errors resulted in DLA GF's Net Position, reported on the financial statements, to be overstated by $44.7 million. DLA GF made adjustments to properly recognize: (1) Internal Use Software in Development placed in service and (2) the classification of intra-agency shared service costs. More specifically:

**Internal Use Software in Development placed in service:** The FY 2022 Internal Use Software (IUS) in Development was corrected to reflect IUS that was placed into service in a prior year. The impact of this error resulted in DLA GF's General Property Plant and Equipment and Cumulative Results of Operations to be overstated by $50.1 million. The correction required prior period adjustments for the FY 2022 Balance Sheet and Statement of Changes in Net Position by decreasing General Property, Plant and Equipment, Net and Cumulative Results of Operations by $50.1 million.

**Classification of intra-agency shared service costs:** In FY 2022, DLA GF included the Agency's $5.4 million in costs for RACER/EII software, as part of the E&DL. In FY 2023, DLA reevaluated the RACER/ EII intra-agency shared service costs paid to USACE and determined the costs should be reported as a recurring operating expense. The correction required prior period adjustments to the FY 2022 Balance Sheet and Statement of Net Costs by decreasing Environmental and Disposal Liabilities and Gross Costs by $5.4 million.

(Refer to Note 1.C., *Departures from U.S. GAAP*, Note 1.I., General Property, Plant, and Equipment, Net, Note 1.N., *Environmental and Disposal Liabilities*, Note 1.R., *Net Position*, and Note 1.T., *Expenses*.)

| Balance Sheet<br>As of September 30, 2022<br>(dollars in thousands) | Unaudited<br>FY 2022<br>Previously<br>Reported | Unaudited<br>FY 2022<br>Adjustments | Unaudited<br>FY 2022<br>Restated |
|---|---|---|---|
| **ASSETS** | | | |
| **Intragovernmental** | | | |
| Fund Balance with Treasury (Note 2) | $ 2,406,663 | $ - | $ 2,406,663 |
| Accounts Receivable (Note 3) | 13,779 | - | 13,779 |
| **Total Intragovernmental Assets** | **2,420,442** | **-** | **2,420,442** |
| **Other than Intragovernmental** | | | |
| Accounts Receivable (Note 3) | 15 | - | 15 |
| Inventory and Related Property, Net (Note 4) | 29,486 | - | 29,486 |
| General Property, Plant and Equipment, Net (Note 5) | 442,378 | (50,127) | 392,251 |
| Advances and Prepayments | 7,741 | - | 7,741 |
| Other Assets | 88 | - | 88 |
| **Total Other than Intragovernmental Assets** | **479,708** | **(50,127)** | **429,581** |
| **TOTAL ASSETS** | **$ 2,900,150** | **$ (50,217)** | **$ 2,850,023** |
| | | | |
| **LIABILITIES (Note 6)** | | | |
| **Intragovernmental** | | | |
| Accounts Payable | $ 21,481 | $ - | $ 21,481 |
| Other Liabilities; | | | |
| Other Current Liabilities-Benefits Program Contributions Payable (Note 7) | 1,306 | - | 1,306 |
| Other Liabilities | - | - | - |
| Total Intragovernmental Other Liabilities | 1,306 | - | 1,306 |
| **Total Intragovernmental** | **22,724** | - | **22,724** |
| **Other than Intragovernmental** | | | |
| Accounts Payable | 56,668 | - | 56,668 |
| Environmental and Disposal Liabilities (Note 8) | 83,777 | (5,431) | 78,346 |
| Federal Employee Benefits Payable (Note 7) | 8,041 | - | 8,041 |
| Advances from Others and Deferred Revenue | 24 | - | 24 |
| Other Liabilities (Note 9) | 3,102 | - | 3,102 |
| **Total Other than Intragovernmental** | **151,612** | **(5,431)** | **146,181** |
| **TOTAL LIABILITIES** | **174,336** | **(5,431)** | **168,905** |
| | | | |
| **Commitments and Contingencies** | | | |
| | | | |
| **NET POSITION** | | | |
| Unexpended Appropriations-Funds from Other than Dedicated Collections | 2,344,480 | - | 2,344,480 |
| Cumulative Results of Operations-Funds from Other than Dedicated Collections | 381,334 | (44,696) | 336,638 |
| **TOTAL NET POSITION** | **2,725,814** | **(44,696)** | **2,681,118** |
| **TOTAL LIABILITIES AND NET POSITION** | **$ 2,900,150** | **$ (50,127)** | **$ 2,850,023** |

| Statement of Net Cost<br>For the Year Ended September 30, 2022<br>(dollars in thousands) | Unaudited<br>FY 2022<br>Previously<br>Reported | Unaudited<br>FY 2022<br>Adjustments | Unaudited<br>FY 2022<br>Restated |
|---|---|---|---|
| **Operations and Maintenance** | | | |
| Gross Cost | $ 425,837 | $ (5,431) | $ 420,406 |
| Less: Earned Revenue | (29,470) | - | (29,470) |
| **Net Cost** | **396,367** | **(5,431)** | **390,936** |
| **Procurement Defense-Wide** | | | |
| Gross Cost | 9,902 | - | 9,902 |
| Less: Earned Revenue | - | - | - |
| **Net Cost** | **9,902** | **-** | **9,902** |
| **Research, Development, Test & Evaluation** | | | |
| Gross Cost | 339,043 | - | 339,043 |
| Less: Earned Revenue | (49,328) | - | (49,328) |
| **Net Cost** | **289,715** | **-** | **289,715** |
| **Family Housing and Military Construction** | | | |
| Gross Cost | 18,200 | - | 18,200 |
| Less: Earned Revenue | - | - | - |
| **Net Cost** | **18,200** | **-** | **18,200** |
| **Gross Cost** | **792,982** | **(5,431)** | **787,551** |
| **Less: Earned Revenue** | **(78,798)** | **-** | **(78,798)** |
| **NET COST OF OPERATIONS** | **$ 714,184** | **$ (5,431)** | **$ 708,753** |

| Statement of Net Position<br>For the Year Ended September 30, 2022<br>(dollars in thousands) | Unaudited<br>FY 2022<br>Previously<br>Reported | Unaudited<br>FY 2022<br>Adjustments | Unaudited<br>FY 2022<br>Restated |
|---|---|---|---|
| **Unexpended Appropriations** | | | |
| Beginning Balances | $ 1,883,232 | $ - | $ 1,883,232 |
| Appropriations Received | 1,419,418 | - | 1,419,418 |
| Appropriations Transferred-in/out | 1,779 | - | 1,779 |
| Other Adjustments | (29,861) | - | (29,861) |
| Appropriations Used | (930,088) | - | (930,088) |
| **Change in Unexpended Appropriations** | **461,248** | **-** | **461,248** |
| **Total Unexpended Appropriations: Ending Balance** | **2,344,480** | **-** | **2,344,480** |
| **Cumulative Results of Operations** | | | |
| Beginning Balances | 521,106 | - | 521,106 |
| Correction of Errors | - | (50,127) | (50,127) |
| Beginning Balances, as Adjusted | 521,106 | (50,127) | 470,979 |
| Other Adjustments | (447) | - | (447) |
| Appropriations Used | 930,088 | - | 930,088 |
| Transfers-in/out Without Reimbursement | (358,018) | - | (358,018) |
| Imputed Financing | 2,789 | - | 2,789 |
| **Net Cost of Operations** | **714,814** | **(5,431)** | **708,753** |
| **Net Change in Cumulative Results of Operations** | **(139,772)** | **5,431** | **(134,341)** |
| **Cumulative Results of Operations: Ending Balance** | **381,334** | **(44,696)** | **336,638** |
| **TOTAL NET POSITION** | **$ 2,725,814** | **$ (44,696)** | **$ 2,681,118** |

# Required Supplementary Information (Unaudited)

## Combining Statements of Budgetary Resources

The Combining Statements of Budgetary Resources combines the availability, status, and outlays of DLA GF budgetary resources. The below tables provide the Combining Statements of the Budgetary Resources disaggregated by DLA GF programs for the years ended September 30, 2023 and 2022, respectively. As the Combining Statements of the Budgetary Resources are prepared at the appropriation level, DLA GF presented the programs by appropriation. However, for reporting purposes, due to the materiality and size of Family Housing, DLA GF combined the Family Housing Program with MILCON in its Statements of Net Cost for presentation purposes.

## Combining Statement of Budgetary Resources

For the Year Ended September 30, 2023 (dollars in thousands)

| | Operation and Maintenance | Procurement Defense-Wide | Research, Development, Test & Evaluation | Family Housing | Military Construction | FY 2023 Total |
|---|---|---|---|---|---|---|
| **BUDGETARY RESOURCES** | | | | | | |
| Unobligated Balance from Prior Year Budget Authority, Net | $ 41,836 | $ 15,724 | $ 123,891 | $ 35 | $ 486,333 | $ 667,819 |
| Appropriations | 419,623 | 24,501 | 356,706 | - | 220,494 | 1,021,324 |
| Spending Authority from Offsetting Collections | 40,656 | - | 49,704 | - | - | 90,360 |
| **TOTAL BUDGETARY RESOURCES** | **$ 502,115** | **$ 40,225** | **$ 530,301** | **$ 35** | **$ 706,827** | **$ 1,779,503** |
| **STATUS OF BUDGETARY RESOURCES** | | | | | | |
| New Obligations and Upward Adjustments | $ 466,102 | $ 23,506 | $ 430,846 | $ - | $ 277,763 | $ 1,198,217 |
| Unobligated Balance, End of Year: | | | | | | |
| Apportioned, Unexpired Accounts | 1,617 | 16,202 | 77,918 | - | 401,481 | 497,218 |
| Unexpired Unobligated Balance, End of Year | 1,617 | 16,202 | 77,918 | - | 401,481 | 497,218 |
| Expired Unobligated Balance, End of Year | 34,396 | 517 | 21,537 | 35 | 27,583 | 84,068 |
| Total Unobligated Balance, End of Year | 36,013 | 16,719 | 99,455 | 35 | 429,064 | 581,286 |
| **TOTAL BUDGETARY RESOURCES** | **$ 502,115** | **$ 40,225** | **$ 530,301** | **$ 35** | **$ 706,827** | **$ 1,779,503** |
| **OUTLAYS, NET** | | | | | | |
| Outlays, Net | **$ 425,954** | **$ 222,842** | **$ 324,868** | **$ 24** | **$ 186,414** | **$ 1,160,102** |
| **AGENCY OUTLAYS, NET** | **$ 425,954** | **$ 222,842** | **$ 324,868** | **$ 24** | **$ 186,414** | **$ 1,160,102** |

# Combining Statement of Budgetary Resources

For the Year Ended September 30, 2022 (dollars in thousands)

| | Operation and Maintenance | Procurement Defense-Wide | Research, Development, Test & Evaluation | Family Housing | Military Construction | FY 2022 Total |
|---|---|---|---|---|---|---|
| **BUDGETARY RESOURCES** | | | | | | |
| Unobligated Balance from Prior Year Budget Authority, Net | $ 22,688 | $ 7,606 | $ 85,131 | $ 337 | $ 495,938 | $ 611,700 |
| Appropriations | 426,830 | 510,896 | 350,004 | - | 137,530 | 1,425,260 |
| Spending Authority from Offsetting Collections | 32,466 | - | 29,468 | - | - | 61,934 |
| **TOTAL BUDGETARY RESOURCES** | **$ 481,984** | **$ 518,502** | **$ 464,603** | **$ 337** | **$ 633,468** | **$ 2,098,894** |
| **STATUS OF BUDGETARY RESOURCES** | | | | | | |
| New Obligations and Upward Adjustments | $ 461,506 | $ 502,829 | $ 354,728 | $ - | $ 169,311 | $ 1,488,374 |
| Unobligated Balance, End of Year: | | | | | | |
| Apportioned, Unexpired Accounts | 694 | 15,420 | 99,769 | - | 451,376 | 567,259 |
| Unexpired Unobligated Balance, End of Year | 694 | 15,420 | 99,769 | - | 451,376 | 567,259 |
| Expired Unobligated Balance, End of Year | 19,784 | 253 | 10,106 | 337 | 12,781 | 43,261 |
| Total Unobligated Balance, End of Year | 20,478 | 15,673 | 109,875 | 337 | 464,157 | 610,520 |
| **TOTAL BUDGETARY RESOURCES** | **$ 481,984** | **$ 518,502** | **$ 464,603** | **$ 337** | **$ 633,468** | **$ 2,098,894** |
| **OUTLAYS, NET** | | | | | | |
| Outlays, Net | $ 396,773 | $ 14,814 | $ 279,349 | $ 271 | $ 220,997 | $ 912,204 |
| **AGENCY OUTLAYS, NET** | **$ 396,773** | **$ 14,814** | **$ 279,349** | **$ 271** | **$ 220,997** | **$ 912,204** |

### Ordnance Offload

Sailors assigned to the USS George H.W. Bush harness ordnance on the flight deck during an ammunition offload with the USNS Supply in the Atlantic Ocean, May 16, 2023. **Photo By:** Navy Petty Officer 3rd Class Nicholas Avis

### DLA Distribution commander visits DLA Distribution Korea

Navy Rear Adm. Grafton D. Chase, Defense Logistics Agency Distribution commander, center, tours the new DLA Distribution Korea warehouse on Camp Carroll, Nov. 16, 2022. **Photo by:** DLA Distribution Public Affairs

# Transaction Fund

**Inspection Time**
Air Force Capt. Bianca Santos conducts a preflight inspection at Kadena Air Base, Japan, April 14, 2023.

**Photo by:** Air Force Senior Airman Jessi Roth

# Audit Reports

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

November 8, 2023

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)/
CHIEF FINANCIAL OFFICER, DOD
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Transmittal of the Independent Auditor's Reports on the Defense Logistics Agency National Defense Stockpile Transaction Fund Financial Statements and Related Notes for FY 2023 and FY 2022
(Project No. D2023-D000FE-0049.000, Report No. DODIG-2024-020)

We contracted with the independent public accounting firm of Ernst & Young, LLP (EY) to audit the Defense Logistics Agency (DLA) National Defense Stockpile Transaction Fund (Transaction Fund) Financial Statements and related notes as of and for the fiscal years ended September 30, 2023, and 2022. The contract required EY to provide a report on internal control over financial reporting and compliance with provisions of applicable laws and regulations, contracts, and grant agreements, and to report on whether the DLA's financial management systems substantially complied with the requirements of the Federal Financial Management Improvement Act of 1996. The contract required EY to conduct the audit in accordance with generally accepted government auditing standards (GAGAS); Office of Management and Budget audit guidance; and the Government Accountability Office/Council of the Inspectors General on Integrity and Efficiency, "Financial Audit Manual," Volume 1, May 2023, Volume 2, May 2023, and Volume 3, June 2023. EY's Independent Auditor's Reports are attached.

EY's audit resulted in a disclaimer of opinion. EY could not obtain sufficient, appropriate audit evidence to support the reported amounts within the DLA Transaction Fund Financial Statements. As a result, EY could not conclude whether the financial statements and related notes were presented fairly and in accordance with Generally Accepted Accounting Principles. Accordingly, EY did not express an opinion on the DLA Transaction Fund FY 2023 and FY 2022 Financial Statements and related notes.

EY's separate report, "Report of Independent Auditors on Internal Control Over Financial Reporting," discusses six material weaknesses related to the DLA's internal controls over financial reporting.* Specifically, EY's report stated that the DLA did not:

- validate and support Inventory balances and transactions;
- reconcile Fund Balance with Treasury;
- support Accounts Payable, expenses, and related budgetary balances;
- design controls over the financial statement reporting process to identify and prevent inaccurate balances and footnotes;
- document end-to-end business processes, monitor internal control risks, and remediate audit findings; or
- ensure the effective design and operation of financial reporting information systems.

EY's additional report, "Report of Independent Auditors on Compliance and Other Matters," discusses two instances of noncompliance with provisions of applicable laws and regulations, contracts, and grant agreements. Specifically, EY's report describes instances in which the DLA's financial management systems did not comply with the Federal Financial Management Improvement Act of 1996 and the Federal Managers' Financial Integrity Act of 1982. EY's report also discusses a potential Antideficiency Act violation that may have occurred when the DLA obligated funding from a multiyear appropriation before its apportionment. The potential violation is currently under formal investigation.

In connection with the contract, we reviewed EY's reports and related documentation and discussed them with EY's representatives. Our review, as differentiated from an audit of the financial statements and related notes in accordance with GAGAS, was not intended to enable us to express, and we do not express, an opinion on the DLA Transaction Fund FY 2023 and FY 2022 Financial Statements and related notes. Furthermore, we do not express conclusions on the effectiveness of internal controls over financial reporting, on whether the DLA's financial systems substantially complied with Federal Financial Management Improvement Act of 1996 requirements, or on

* A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting that results in a reasonable possibility that management will not prevent, or detect and correct, a material misstatement in the financial statements in a timely manner.

compliance with provisions of applicable laws and regulations, contracts, and grant agreements. Our review disclosed no instances where EY did not comply, in all material respects, with GAGAS. EY is responsible for the attached November 8, 2023 reports and the conclusions expressed within the reports.

We appreciate the cooperation and assistance received during the audit. If you have any questions, please contact me.

FOR THE INSPECTOR GENERAL:

Lorin T. Venable, CPA
Assistant Inspector General for Audit
Financial Management and Reporting

Attachments:
As stated

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# Report of Independent Auditors

The Director of the Defense Logistics Agency and the
Inspector General of the Department of Defense

## Report on the Audit of the Financial Statements

### *Disclaimer of Opinion*

We were engaged to audit the financial statements of the National Defense Stockpile Transaction Fund of the Defense Logistics Agency (DLA), which comprise the balance sheets as of September 30, 2023 and 2022, and the related statements of net cost and changes in net position and statements of budgetary resources for the years then ended, and the related notes (collectively referred to as the "financial statements").

We do not express an opinion on the accompanying financial statements of DLA. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

### *Basis for Disclaimer of Opinion*

DLA continues to have unresolved accounting issues and material weaknesses in internal controls that cause DLA to be unable to provide sufficient evidential support for complete and accurate financial statements on a timely basis. As a result of these matters, we were unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded balances and the elements making up DLA's financial statements as of and for the years ended September 30, 2023 and 2022.

### *Departures from U.S. Generally Accepted Accounting Principles*

As described in Note 1, DLA has not implemented certain accounting standards for the Department of Defense and the federal government. The effect of these matters on DLA's financial statements as of and for the years ended September 30, 2023 and 2022 is not currently determinable by DLA and could be material.

### *Responsibilities of Management for the Financial Statements*

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and

fair presentation of the financial statements that are free of material misstatement, whether due to fraud or error.

***Auditor's Responsibilities for the Audit of the Financial Statements***

Our responsibility is to conduct an audit of DLA's financial statements in accordance with auditing standards generally accepted in the United States of America, in accordance with the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States (*Government Auditing Standards*), and in accordance with the provisions of Office of Management and Budget Bulletin No. 24-01, *Audit Requirements for Federal Financial Statements*, and to issue an auditor's report. However, because of the matters described in the Basis for Disclaimer of Opinion section of our report, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

We are required to be independent of DLA and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audit.

***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Required Supplementary Information, as listed in the Table of Contents, be presented to supplement the financial statements. Such information is the responsibility of management and, although not a part of the financial statements, is required by the Federal Accounting Standards Advisory Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We were unable to apply certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report. We do not express an opinion or provide any assurance on the information.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we also have issued our reports dated November 8, 2023, on our consideration of DLA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of those reports is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of DLA's internal control over financial

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reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DLA's internal control over financial reporting and compliance.

Ernst & Young LLP

November 8, 2023

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# Report of Independent Auditors on Internal Control Over Financial Reporting Based on an Engagement to Audit the Financial Statements Performed in Accordance with *Government Auditing Standards*

The Director of the Defense Logistics Agency and the
Inspector General of the Department of Defense

We were engaged to audit, in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States (*Government Auditing Standards)* and the provisions of Office of Management and Budget (OMB) Bulletin No. 24-01, *Audit Requirements for Federal Financial Statements,* the financial statements of the National Defense Stockpile Transaction Fund of the Defense Logistics Agency (DLA), which comprise the balance sheet as of September 30, 2023, and the related statements of net cost and changes in net position and statement of budgetary resources for the year then ended, and the related notes (collectively referred to as the "financial statements"), and have issued our report thereon dated November 8, 2023. Our report disclaims an opinion on the financial statements because DLA continues to have unresolved accounting issues and material weaknesses in internal controls that cause DLA to be unable to provide sufficient evidential support for complete and accurate financial statements on a timely basis.

## Report on Internal Control Over Financial Reporting

In connection with our engagement to audit the financial statements, we considered DLA's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of DLA's internal control. Accordingly, we do not express an opinion on the effectiveness of DLA's internal control. We did not consider all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA), such as those controls relevant to preparing performance information ensuring efficient operations.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as described below and in more detail in Appendix A, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a

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combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described below and in Appendix A as items I through VI to be material weaknesses.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described below and in Appendix B as items I and II to be significant deficiencies.

**Material Weaknesses**

We identified the following matters involving internal control over financial reporting and its operation that we consider to be material weaknesses, as defined above:

I. Inventory – Inventory is comprised of strategic and critical materials that can be used in times of national emergencies. The materials include ores, metals, alloys, chemicals, high-performance fibers and energetics. Policies, procedures and internal controls surrounding documentation of procurements and disbursements, validating the perpetual inventory systems by performing periodic physical counts, accumulating cost of inventory, and supporting inventory balances and transactions all had deficiencies. The combination of these deficiencies in aggregate results in a material weakness in internal control related to inventory. The matters identified related to inventory are further described in Appendix A.

II. Fund Balance with Treasury (FBwT) – FBwT represents the aggregate amount of funds in DLA's account with U.S. Treasury. DLA was unable to reconcile FBwT beginning and ending balances from the general ledger to U.S. Treasury and support the FBwT balance. DLA implemented a process to reconcile the collection and disbursement activity from the general ledger to U.S. Treasury, however, DLA did not implement controls to assess the completeness and accuracy of the source data used in the reconciliation. DLA lacked policies, procedures and controls to evaluate the impact to FBwT for transactions in suspense accounts and the Statement of Differences (SOD). The combination of these deficiencies in aggregate results in a material weakness in internal control related to FBwT. The matters identified related to FBwT are further described in Appendix A.

III. Accounts Payable (AP) and Expense – AP represents the amount owed to third parties by DLA for goods and services received. Expenses are incurred and recognized when DLA receives goods and services from the public or other federal entities. DLA was unable to support the AP balance, expenses and related budgetary beginning balances. In addition, DLA did not have adequate policies, procedures and internal controls for the procure to pay process, including the process to create and approve obligations and the process to review, record and pay invoices. Furthermore, DLA lacked adequate procedures to record obligations and accrue for liabilities incurred but not paid, and it recorded transactions in the procure to pay process in incorrect periods. The combination of these deficiencies in aggregate results

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in a material weakness in internal control related to AP and expense. The matters identified related to AP and expense are further described in Appendix A.

IV. Financial Reporting – Financial reporting encompasses all aspects of operations affecting DLA's ability to produce reliable financial statements and disclosures in accordance with U.S. generally accepted accounting principles (GAAP). DLA's financial statement preparation process lacked sufficient controls to review and identify inaccurate balances within the financial statements and incomplete or inaccurate footnote disclosures. In addition, DLA lacked policies and procedures to validate account balances and monitor reporting variances between source systems, resulting in DLA recording unsupported journal vouchers (JVs) to correct the variances. Furthermore, DLA was unable to provide detailed listings for budgetary accounts that reconcile to the general ledger. The combination of these deficiencies in aggregate results in a material weakness in internal control related to financial reporting. The matters identified related to financial reporting are further described in Appendix A.

V. Oversight and Monitoring – Oversight and monitoring relate to DLA's lack of establishment and implementation of a sufficient enterprise-wide control environment as required by OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management Internal Control*. DLA did not have an effective OMB Circular A-123 program, which impacted DLA's ability to appropriately identify and address significant risks for all key business processes. DLA did not implement appropriate internal controls, including the documentation of policies and procedures that describe DLA's environment related to end-to-end business processes, monitoring of service providers, related parties, systems, risks, controls and remediation of audit findings. In addition, DLA did not perform a proper review of data/reports used in the execution of key controls. The combination of these deficiencies in aggregate results in a material weakness in internal control related to oversight and monitoring. The matters identified related to oversight and monitoring are further described in Appendix A.

VI. Information Systems – Our assessment of DLA's information technology (IT) controls and the computing environment identified deficiencies which, collectively, constitute a material weakness in the design and operation of information systems controls over financial data. Based on our review, we identified five areas of deficiency which, when aggregated, result in a material weakness. The deficiencies relate to the following five areas:

- Access Controls
- Configuration Management
- Segregation of Duties Controls
- Security Management/Governance Over Implementation of Security Controls
- IT Operations

The matters identified related to information systems are further described in Appendix A.

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**Significant Deficiencies**

We identified the following matters involving internal control over financial reporting and its operation that we consider to be significant deficiencies, as defined above:

I. Revenue – Revenue is earned when DLA sells goods to the public. DLA lacked adequate policies, procedures and controls to ensure that revenue and cost of goods sold are recorded in accordance with U.S. GAAP. The matters identified related to revenue are further described in Appendix B.

II. Environmental Liabilities (EL) – ELs are comprised of cleanup costs associated with the restoration of sites on real property that DLA manages. DLA lacked adequate controls to evaluate the completeness and measurement of the ELs and the ELs recorded in the financial statements. The matters identified related to EL are further described in Appendix B.

***DLA's Response to Findings***

*Government Auditing Standards* require the auditor to perform limited procedures on DLA's response to the findings identified in our engagement to audit and described in the accompanying Management's Response to Audit Reports dated November 8, 2023. DLA's response was not subjected to the other auditing procedures applied in the engagement to audit the financial statements and, accordingly, we express no opinion on the response.

***Purpose of This Report***

The purpose of this report is solely to describe the scope of our testing of internal control and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control. This report is an integral part of an engagement to perform an audit in accordance with *Government Auditing Standards* in considering the entity's internal control. Accordingly, this communication is not suitable for any other purpose.

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**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2023 on our tests of DLA's compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DLA's compliance.

Ernst + Young LLP

November 8, 2023

## Appendix A – Material Weaknesses

### I. Inventory

DLA's inventory is comprised of strategic and critical materials that can be used in times of national emergencies. The materials include ores, metals, alloys, chemicals, high-performance fibers and energetics. In accordance with FMFIA, management is responsible for establishing effective controls over and accountability for all assets for which the agency is responsible. DLA's controls and processes did not exist or were not operating in several significant areas, specifically:

A. **Lack of or Inadequate Policies, Procedures and Controls Over Inventory Processes.** DLA lacked or did not have adequate policies, procedures and controls, including the design of controls, over the following:
   - **Physical Inventory Counts.** DLA did not adequately design controls over physical inventory counts. Adjustments for variances identified during inventory counts were not properly evaluated, which includes assessing the impact of the variances to the remaining inventory balance, and were not reviewed for completeness and accuracy. Variance thresholds were established only by using the weight discrepancies without considering the monetary impact. As such, weight discrepancies below the threshold may be a material error and not adjusted in the general ledger and the financial statements.
   - **Inventory Recorded in the Appropriate Period.** DLA did not have policies and procedures in place to record transactions in the period that the transaction occurred or to accrue for transactions that occurred but were not posted at period-end.

B. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** DLA did not have policies, procedures and controls to effectively implement accounting standards, causing an inaccurate presentation of inventory on the balance sheet and in the related footnote disclosure. Specifically, DLA neither implemented nor applied the costing and valuation methodologies set forth by Statement of Federal Financial Accounting Standards (SFFAS) No. 3, *Accounting for Inventory and Related Property* and SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials*. For example:
   - SFFAS No. 3 states that entities should value inventory on the basis of historical cost. DLA was unable to support the valuation of inventory at historical cost as required by SFFAS No. 3 and should apply the alternative valuation methods provided under SFFAS No. 48 to establish the value of inventory at the beginning of the reporting period. DLA had not implemented SFFAS No. 48, and, as such, was unable to support that inventory was valued in accordance with U.S. GAAP.
   - SFFAS No. 3 states that the carrying amount of inventory that has suffered a permanent decline in value to an amount less than the cost should be reduced to the expected net realizable value of the materials. DLA did not have defined policies, procedures and controls to determine whether there were permanent declines in value. For example, DLA did not have documentation that describes the valuation process, including the criteria used

to determine whether a decline in value was temporary or permanent. In addition, the impairment assessment did not include procedures to perform a periodic review and to document the basis for determining that the benchmarks and inputs used for assessing whether a decline in value had occurred were appropriate.

- SFFAS No. 3 states that historical cost shall include all appropriate purchase, transportation and production costs incurred to bring the items to their current condition and location. DLA did not have sufficient policies and procedures to identify and capitalize all appropriate costs incurred in acquiring inventory. In addition, inventory received from other federal agencies was not properly valued and recorded in accordance with SFFAS No. 3.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Lack of or Inadequate Policies, Procedures and Controls Over Inventory Processes.**
   - **Physical Inventory Counts.** Design and implement controls over physical inventory counts. The controls should be designed to review adjustments recorded for completeness and accuracy and to assess the monetary impact of variances, individually and in the aggregate across the entire inventory balance.
   - **Inventory Recorded in the Appropriate Period.** Design and implement policies and procedures, including controls, to process and post transactions to the correct period in the general ledger and that an accrual is recorded at period-end for transactions that should be posted to reflect recording in the proper period but have not been resolved.

B. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** Design policies and procedures to implement the accounting standard, SFFAS No. 3 and SFFAS No. 48. The policies and procedures should consider:
   - Applying the alternative valuation methods provided under SFFAS No. 48 and ensuring that all reporting and disclosure requirements relating to implementation of SFFAS No. 48 are met and that policies and procedures are sufficient to record and present inventory completely and accurately in accordance with SFFAS No. 3 subsequent to implementation of SFFAS No. 48.
   - Determining the criteria for when a decline in value should be considered temporary or permanent, how the market value of specific commodities should be selected and performed, and what benchmarks are used to determine market value.
   - Ensuring that costs to bring inventory to its current condition and location are properly capitalized and that inventory received from federal entities without reimbursement is properly valued in accordance with U.S. GAAP.

## II. Fund Balance with Treasury

Fund Balance with Treasury (FBwT) represents the aggregate amount of funds in DLA's account with U.S. Treasury. Treasury's Financial Manual (TFM) Chapter 5100, Section 5125 requires agencies to implement effective and efficient reconciliation processes and perform timely reconciliations. However, deficiencies existed related to DLA's processes of recording and reconciling transactions involving FBwT.

A. **Lack of or Inadequate Documentation of FBwT Accounting Policies, Procedures and Controls.** DLA did not document the end-to-end process to account for, monitor and report FBwT and FBwT related transactions.
   - **Suspense Accounts.** The documentation did not include the process to reconcile and resolve the amounts recorded in suspense accounts.
   - **Reconciling Items to Treasury.** The documentation did not include the process to research and resolve differences between U.S. Treasury, disbursing system records and accounting system records within a timely basis.

B. **Lack of Controls for the Reconciliation of FBwT Between the General Ledger and the U.S. Treasury.** DLA lacked or did not have adequate controls, including the design of controls, to reconcile FBwT. As a result, DLA was unable to accurately reconcile the beginning and ending general ledger balances to U.S. Treasury.
   - **Statement of Differences (SOD) and Suspense.** DLA had not effectively designed controls to completely and accurately reconcile FBwT. Specifically, DLA had not demonstrated how the differences included in the SODs and suspense accounts were appropriately identified and cleared to the TF.

C. **Lack of or Inadequate Documentation to Substantiate FBwT.** DLA was unable to provide documentation to support the existence and completeness of FBwT. Specifically, documentation was not available to support the composition of a $333 million summary journal voucher and demonstrate that the amount was appropriate to include in FBwT.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation of FBwT Accounting Policies, Procedures and Controls.** Finalize the documentation of the end-to-end process for FBwT. The documentation should include the process to perform regular and recurring reconciliations of the suspense account data and the process to research and resolve differences between U.S. Treasury, disbursing system records and accounting system records within a timely basis.

B. **Lack of Controls for the Reconciliation of FBwT Between the General Ledger and the U.S. Treasury**
   - **SODs and Suspense.** Design and implement procedures to completely and accurately reconcile FBwT, including demonstrating that the differences included in the SODs and suspense accounts associated to the DLA TF are recorded correctly and timely in the general ledger.

C. **Lack of or Inadequate Documentation to Substantiate FBwT.** Develop documentation to support the existence and completeness of FBwT and demonstrate that amounts recorded are appropriate to include in FBwT.

**III. Accounts Payable and Expenses**

Accounts payable (AP) consists of amounts owed to vendors. Expenses are incurred and recognized when DLA obtains goods and services from the public or other federal entities. Undelivered Orders (UDOs) represent the amount of goods and/or services ordered which have not been received. AP, expenses and UDOs fall within the scope of DLA's procure to pay process. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls that provide reasonable assurance that expenses and budgetary transactions applicable to the agency's operations are properly recorded and accounted for to permit the preparation of reliable financial reports. Because of the nature of the operations, DLA has a significant volume of transactions to procure goods and services to sell to its customers. Deficiencies existed in DLA's processes for recording and supporting accounts payable, expenses and the related budgetary balances; recording transactions in the proper period; accruing for liabilities incurred but not yet invoiced; documenting policies, procedures and controls in a sufficient manner; and designing and executing controls over the process to create and approve obligations and to review, record and pay invoices.

A. **Lack of or Inadequate Documentation of UDOs, AP and Expenses Accounting Policies, Procedures and Controls.** DLA did not document the end-to-end processes to account for UDOs, AP and expense transactions.
   - **UDOs.** The documentation did not include the process to review the validity of significantly aged UDOs.
   - **AP.** The documentation did not include the process to evaluate the validity of AP, including significantly aged AP and negative payables; and the process to pay invoices timely or assess interest penalties for late payments in accordance with the Prompt Payment Act.

B. **Lack of or Inadequate Controls Over UDOs, AP, Expense and Cash Disbursement Processes.** DLA lacked or did not have adequate controls, including the design of controls, over the following:
   - **UDOs.** DLA lacked controls to approve and record obligations in a timely manner; controls to record upward and downward adjustments to UDOs accurately and timely; controls to

close invalid UDOs in a timely manner; and controls to review that the purchase order information was recorded accurately in order to record the obligation in the correct period.

- **Vendor Contracts.** DLA lacked controls to execute contracts in accordance with the Federal Acquisition Regulation (FAR), and record obligations timely for contracts, including Indefinite Quantity Contracts (IQC).
- **AP and Cash Disbursements.** DLA lacked controls to post goods receipts in a timely manner and; review invoices prior to payment.
- **Expenses Recorded in the Appropriate Period.** DLA lacked controls to record expense transactions appropriately and accurately in the period that the transaction occurred. As a result, expense transactions were recorded in the incorrect period.
- **Transactions Recorded at the Detailed Level.** DLA lacked controls to comply with the Federal Financial Management Improvement Act (FFMIA), which requires transactions to be recorded at the detailed level. DLA recorded transactions at a summary level for certain budgetary and proprietary accounts. As a result, each summary-level record contained multiple individual transactions. A reconciliation was not performed between detailed transactions posted to the proprietary accounts and the summarized postings to the corresponding budgetary accounts.

C. **Lack of or Inadequate Documentation to Substantiate AP and Expense Transactions.** DLA was unable to provide documentation to support the existence of AP balances, or that expense transactions that occurred were accurately recorded in the financial statements. Specifically, documentation was not available to support the transactions and balances for various accounts, such as accounts payable, negative payables, expenses, UDOs, and upward and downward adjustments to UDOs. For example, DLA was unable to provide sufficient documentation demonstrating that goods received were recorded in the proper period for one purchase order sample selected.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** DLA did not have policies, procedures and controls to effectively implement accounting standards. Specifically, DLA had neither implemented nor applied the accounting set forth by SFFAS No. 1, *Accounting for Selected Assets and Liabilities*, SFFAS No. 4, *Managerial Cost Accounting Standards and Concepts* and SFFAS No. 5, *Accounting for Liabilities of the Federal Government.* For example:

- DLA inappropriately expensed costs that should have been capitalized. For example, inventory purchased for resale was inappropriately expensed.
- DLA processes allow for payment without receipt, thus resulting in a negative payable balance. This occurs when payment is made prior to the goods receipts being posted in the general ledger. This results in an understatement of expenses and payables and a misstatement of UDOs.
- AP and accrued liabilities were not recorded appropriately. For example, DLA applied the straight-line method to calculate the accrual amount but did not perform any assessment to determine whether this was an appropriate methodology. Particularly, for Military

Interdepartmental Purchase Requests (MIPRs) that do not have a fixed monthly cost, the straight-line method was not appropriate.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation of UDOs, AP and Expenses Accounting Policies, Procedures and Controls.** Update and finalize the process cycle memoranda that document the end-to-end processes for UDOs, AP and expenses.
   - **UDOs.** The documentation should include the process to review the validity of significantly aged UDOs, including a process to write off residual UDOs for completed transactions.
   - **AP.** The documentation should include the process to evaluate the validity of accounts payable, including significantly aged AP and negative payables, and the process to pay invoices timely or assess interest penalties for late payments in accordance with the Prompt Payment Act.

B. **Lack of or Inadequate Controls Over UDOs, AP, Expenses and Cash Disbursement Processes.**
   - **UDOs.** Design and implement controls to approve and record obligations in a timely manner; controls to record upward and downward adjustments to UDOs accurately and timely; controls to review and close invalid UDOs in a timely manner; and controls to validate that the purchase order information is recorded accurately in order to record the obligation in the correct period.
   - **Vendor Contracts.** Design and implement controls to execute contracts in accordance with the FAR and record obligations timely for contracts, including IQCs. For example, controls that prevent contracts from being completed and executed without the appropriate terms and conditions required by the FAR.
   - **AP and Cash Disbursements.** Design and implement controls to post goods receipts in a timely manner and review invoices prior to payment.
   - **Expenses Recorded in the Appropriate Period.** Design and implement controls to record expense transactions appropriately and accurately in the period that the transaction occurred and controls to monitor expense transactions at or near period-end.
   - **Transactions Recorded at the Detailed Level.** Design and implement controls to comply with the FFMIA and reconcile the transaction-level detail to the summarized postings in each account.

C. **Lack of or Inadequate Documentation to Substantiate AP and Expense Transactions.** Develop documentation to support that AP balances exist, or that expense transactions occurred and are accurately recorded in the financial statements.

D. **Lack of Policies, Procedures and Controls to Effectively Implement Accounting Standards.** Design and implement policies and procedures to record expenses incurred in the proper period and to properly classify costs and payables in accordance with SFFAS No. 1, SFFAS No. 4 and SFFAS No. 5.

## IV. Financial Reporting

Financial reporting encompasses all aspects of operations affecting DLA's ability to produce reliable financial statements and disclosures. This process starts with establishing an effective governance structure to identify and assess risk and continues with developing a control environment that is effective and efficient to manage identified risks. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls to achieve reliable financial reporting. However, deficiencies existed in DLA's processes related to the accumulation and presentation of their financial position and results of operations.

A. **Lack of or Inadequate Documentation of Financial Reporting and Budgetary Policies, Procedures, and Controls.** DLA did not document the end-to-end process related to financial reporting and funds management.
   - **Financial Reporting**. The documentation did not include the processes to review and reconcile system generated reversals of prior year JVs which impact opening balances.
   - **Funds Management**. The documentation did not sufficiently include a description of the process to record budget authority, the transfer process, and the Treasury warrant process.

B. **Lack of Controls Over Compliance with the TFM United States Standard General Ledger (USSGL).** DLA did not have controls to configure the general ledger posting logic to be compliant with the USSGL and apply TFM updates timely, nor did DLA have controls to link business events to the correct posting logic. As a result, transactions were not recorded appropriately. For example, DLA inappropriately used a general ledger account (negative payables) to track payments made without goods received and inappropriately combined entries to record the movement of budgetary funds through the apportionment and allotment process, which should be recorded separately. Furthermore, DLA did not implement the TFM update to add USSGL account 425400 – Reimbursements and Other Income Earned – Collected From Non-Federal Sources. In addition, the posting logic for various inventory transactions, such as goods being sold and returned into inventory, did not meet the corresponding TFM business events.

C. **Lack of or Inadequate Controls Over Financial Reporting Processes**. DLA lacked or did not have adequate controls, including the design of controls, over the following:
   - **Beginning Balances for Budgetary Accounts.** DLA did not have controls to verify the accuracy of the beginning balances for budgetary accounts, such as the Total Actual Resources Collected account.
   - **Budgetary Resources**. DLA did not have adequately designed controls, including monitoring of budgetary processes performed by the Office of the Under Secretary of

Defense – Comptroller (OUSD-C), to prevent or detect obligations incurred prior to or in excess of available budgetary resources. As a result, in FY 2023, DLA incurred obligations in excess of apportioned authority.

- **Trading Partner Transactions.** DLA did not have controls in place to validate and reconcile trading partner eliminations. Adjustments made to accounts payable, expenses and undisbursed funds were not appropriately supported. A complete reconciliation was not performed at the agreement level to the trading partner adjustments that were being made. As a result, trading partner adjustments were recorded in the Defense Departmental Reporting System (DDRS) as "top-side" adjustments and were identified as "unsupported" by DFAS.
- **Contingent Liabilities.** Controls that were implemented were not adequately designed as they did not include sufficient procedures to verify the data used to assess contingent liabilities were complete and accurate.
- **Financial Statement Close Process.** DLA did not have adequately designed controls around the annual close and reconciliation processes, such as the following: the monthly or quarterly reconciliation between the unadjusted trial balance (UTB) and the adjusted trial balance (ATB) was not performed sufficiently and timely and did not consider system generated JVs; the information used in the reconciliation of UTB to ATB was not complete and accurate; and the review of the procedures performed during the financial statement close process was not adequate.
- **Budgetary to Proprietary Tie Points.** DLA did not have adequately designed controls around the tie-point process. There were reconciliation issues between the budgetary and proprietary tie points. As a result, DFAS recorded unsupported monthly and quarterly JVs in the general ledger and Defense Departmental Reporting System (DDRS) to reconcile DLA's budgetary accounts to the proprietary accounts.
- **Monthly or Quarterly JV Adjustments.** DLA did not have controls to review and approve JV adjustments recorded in the general ledger and DDRS by DLA and DFAS for completeness, accuracy and validity. As a result, a comprehensive listing of adjustments made was not maintained to allow DLA to determine the appropriateness of each JV adjustment, including those recorded by their service provider.
- **Financial Statement Review Process.** The level of review of the financial statements and footnote disclosures was insufficient to detect and correct misstatements in the financial statements and related disclosures. As a result, inaccurate balances and disclosures were reported in the financial statements and notes. For example, line items were not appropriately classified between federal and with the public; supporting documentation did not support the balances recorded in the notes; and the financial statements were not prepared in conformity with U.S. GAAP as described in Note 1, Significant Accounting Policies, which did not sufficiently describe changes or noncompliance in U.S. GAAP reporting. In addition, DLA had not designed processes or controls to implement new accounting standards. As a result, DLA had not implemented accounting standards such as SFFAS No. 49, *Public-Private Partnerships: Disclosure Requirements.*
- **Transactions Recorded Using Elevated Privileges.** DLA did not have controls to review and approve transactions recorded with elevated access privileges.

D. **Lack of or Inadequate Documentation to Substantiate Budgetary Amounts.** DLA was unable to provide documentation to support the existence and completeness of Total Actual Resources Collected and Unapportioned Authority. Specifically, documentation was not available to support the composition of a $333 million summary journal voucher and demonstrate that the amount was appropriate to include in Total Actual Resources Collected and Unapportioned Authority. In addition, DLA was unable to provide detailed listings for budgetary accounts at the purchase order (PO) or sales order (SO) level that reconcile to the general ledger, such as delivered and undelivered orders and unfilled customer orders.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation of Financial Reporting and Budgetary Policies, Procedures, and Controls.**
   - **Financial Reporting**. Document the financial reporting process, to accurately reflect all aspects of the end-to-end process, including processes and controls performed to reconcile prior year activity to opening balances.
   - **Funds Management.** Document the funds management process and controls to accurately reflect all aspects of the end-to-end budget to execute process, including process and controls performed by DLA and service providers.

B. **Lack of Controls over Compliance with the TFM United States Standard General Ledger (USSGL).** Design and implement controls that: configure posting logic in the general ledger to be compliant with the USSGL; apply TFM updates in a timely manner; link business events to the correct posting logic; and post transactions as intended.

C. **Lack of or Inadequate Controls over Financial Reporting Processes.**
   - **Beginning Balances for Budgetary Accounts.** Design and implement control activities to accurately state the beginning balance for carryforward budgetary accounts.
   - **Budgetary Resources**. Design and implement controls to ensure budgetary resources are appropriately apportioned in order to prevent and detect obligations from being incurred against appropriations that have not been apportioned from OMB.
   - **Trading Partner Transactions.** Design and implement controls to perform a reconciliation at the agreement level to validate trading partner eliminations, which includes identifying, researching and resolving variances between DLA general ledger data and trading partners.
   - **Contingent Liabilities.** Enhance control activities to verify the completeness and accuracy around system generated reports used in the execution of controls to identify, estimate, record and disclose contingent liabilities in the financial statements.
   - **Financial Statement Close Process.** Develop and implement controls around the annual close and reconciliation process, which includes a complete, accurate and timely

reconciliation of the UTB to the ATB. And processes and controls to analyze the impact of and implement new accounting standards, as appropriate.

- **Budgetary to Proprietary Tie Points.** Design and implement controls to reconcile budgetary to proprietary tie points and investigate variances.
- **Monthly or Quarterly JV Adjustments.** Design and implement controls to review and approve JV adjustments recorded in the general ledger and DDRS by DLA and DFAS for completeness, accuracy and validity prior to posting.
- **Financial Statement Review Process.** Design and implement controls to sufficiently review the quarterly and annual financial statements and disclosures; to detect and correct misstatements; to review that the financial statements and disclosures are complete and prepared in accordance with U.S. GAAP; and to analyze the impact of and implement new accounting standards, as appropriate.
- **Transactions Recorded Using Elevated Privileges.** Design and implement controls to review and approve transactions recorded with elevated access privileges to assess for completeness, accuracy and validity. The review and approval should be performed by authorized individuals such as financial management.

D. **Lack of or Inadequate Documentation to Substantiate Budgetary Amounts.** Develop documentation to support the existence and completeness of budgetary amounts and demonstrate that these amounts are appropriate to include in the balance. Develop and implement procedures to generate complete and accurate listings of budgetary accounts at the PO and SO level that reconcile to the general ledger.

## V. Oversight and Monitoring

Oversight and monitoring relate to DLA's lack of establishment and implementation of a sufficient enterprise-wide control environment as required by OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management Internal Control*.

A. **Lack of or Inadequate Documentation Around the OMB A-123 Program**. DLA did not document the end-to-end process to oversee and monitor the enterprise-level risks and controls, including their OMB A-123 program. Specifically, DLA had not performed and documented a sufficient risk assessment at the enterprise and business process level to assess and document reporting matters, such as the complexity of programs, accounting estimates, related party transactions and extent of manual processes; a complete and accurate population of its assessable units, business processes and relevant controls that are responsive to and mitigate risks, including fraud risks; and an assessment and plan for timely remediation of audit findings.

B. **Lack of or Inadequate Controls Around System Generated Reports.** DLA lacked or did not have adequate controls to verify the accuracy and completeness of system generated reports required in the execution of controls.

C. **Insufficient Oversight and Monitoring of Third-Party Service Providers.** Service organizations undergo examinations of internal controls over systems and processes supporting their customers. The results of these examinations are documented in System and Organization Controls 1 (SOC 1) reports and include the independent service auditor's report, the service organization's management assertions and identified Complementary User Entity Controls (CUECs) that users of the service organization (e.g., DLA) should have in place to supplement the service organization's internal controls. DLA did not perform sufficient oversight and monitoring of SOC 1 reports and did not sufficiently design, implement or monitor CUECs over its service providers.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Lack of or Inadequate Documentation Around the OMB A-123 Program.** Document the end-to-end process to oversee and monitor the enterprise-level risks and controls, including the OMB A-123 program. Perform and document a sufficient risk assessment at the enterprise and business process level to assess and document reporting matters. Document a complete and accurate population of its assessable units and business processes. Identify and assess the risks in each business process and design and implement relevant controls that are responsive to and mitigate these risks, including fraud risks. Perform an assessment of audit findings and establish and execute the plan to remediate the audit findings timely.

B. **Lack of or Inadequate Controls Around System Generated Reports.** Design and implement controls to verify the accuracy and completeness around system generated reports used in the execution of controls. For example, the procedures should include footing system generated reports; performing a tie-out of system generated reports to the general ledger; verifying that the parameters used to generate the reports or data are appropriate; selecting a sample of transactions or balances in the report; and validating that the transactions are accurate.

C. **Insufficient Oversight and Monitoring of Third-Party Service Providers.** Design and implement controls around the SOC 1 review process and validate that CUECs are properly identified, designed and operating effectively.

## VI. Information Systems

Information systems controls are a critical component of the federal government's operations to manage the integrity, confidentiality and reliability of its programs and activities and assist with reducing the risk of errors, fraud or other illegal acts. Information management security, access controls, segregation of duties, configuration management, and IT operations controls are fundamental to the integrity of financial data and can help manage risks such as unauthorized access, changes to critical data, and prevent compromised data. The nature, size and complexity of DLA's operations require DLA to administer its programs under a decentralized business model by using numerous geographically dispersed operating locations and complex, extensive information systems.

Control deficiencies in the design and operation of financially significant information systems continue to occur in the information systems environment controls. The deficiencies relate to the following areas:

- Access controls
- Configuration management controls
- Segregation of duties controls
- Security management/governance over implementation of security controls
- IT operations controls

### Access Controls

Access controls include those related to protecting system boundaries, user identification and authentication, authorization, protecting sensitive system resources, audit and monitoring, and physical security. When properly implemented, access controls can help ensure that critical systems assets are physically safeguarded and that logical access to sensitive computer programs and data is granted to users only when authorized and appropriate. Weaknesses in such controls can compromise the integrity of sensitive data and increase the risk that such data may be inappropriately used and disclosed.

The identified access control weaknesses in aggregate represent a significant risk to the DLA financial statements, Information Technology (IT) environment and financial applications. Absent or ineffective preventative controls and compensating detective controls expose financial systems and financial data to inappropriate access, unauthorized inputs and inaccurate entries, resulting in significant risk to the financial statements.

The identified access control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- For a selection of users of financially significant applications, access was not restricted to authorized users with a business need, was not reviewed and documented prior to provisioning, and was not assigned in accordance with the principle of least privilege.
- For a selection of account management controls for financially significant applications, user

access and activity were not monitored and tracked for routine access recertification, revalidation of privileged access and terminated or inactive users.
- For a selection of audit logging controls for one financially significant application, audit logs, security violations and sensitive user activity were not tracked, monitored, resolved or configured appropriately within systems.

### Configuration Management Controls

Configuration management involves the identification and management of security features for all hardware and software components of an information system at a given point and systematically controls changes to that configuration during the system's life cycle. By implementing configuration management controls, DLA can ensure that only authorized applications and software programs are placed into production through establishing and maintaining baseline configurations and monitoring changes to these configurations. Weaknesses in such controls can compromise the integrity of sensitive data and increase the risk that such data may be inappropriately used and disclosed.

The identified configuration management and change control weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls expose financial systems and financial data to unexpected impact from changes, inappropriate or unauthorized changes, and application errors in production.

The identified change control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- For a selection of changes to one financially significant application, both routine and emergency changes were not reviewed, approved and tested in a non-production environment prior to release. The impact and functionality of configuration changes were not assessed prior to implementation.
- For one financially significant application, system configurations, baseline code and production environments were not monitored and inspected for unauthorized changes.
- For one financially significant application, users had access privileges enabling them to bypass the configuration management process and make changes directly to production.

### Segregation of Duties Controls

An effective control environment guards against a particular user having incompatible functions within a system. Segregation of duties controls provide policies, procedures and an organizational structure to prevent one or more individuals from controlling key aspects of computer-related operations and, thereby, conducting unauthorized actions or gaining unauthorized access to financial management information systems.

The identified segregation of duties and conflicting role weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications.

Absent or ineffective controls around segregation of duties allows users to circumvent processes and automated controls in place, obtain unnecessary or elevated access, and impact the integrity of financial data.

The identified weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- Segregation of duties within the user provisioning process were not completed consistently across financially significant applications. Conflicting roles were not inspected and rationalized prior to provisioning. Management did not periodically monitor segregation of duties conflicts that consider both IT and business process roles and activities.
- Application program management has not completely identified sensitive (financial transactions) roles in order to implement appropriate segregation of duties processes and controls.

**Security Management / Governance Over Implementation of Security Controls**

An entity-wide information security management and internal control program is the foundation of a security control structure to address security risks. The security management program should establish a framework and continuous cycle of activity for assessing risk, developing and implementing effective security procedures and monitoring the effectiveness of these procedures. Without a well-designed program, security controls may be inadequate; responsibilities may be unclear, misunderstood or improperly implemented; and controls may be inconsistently applied. Such conditions may lead to insufficient protection of sensitive or critical resources and disproportionately high expenditures for controls over low-risk resources.

The identified security management and governance weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls around internal controls and governance compound data integrity risk by not monitoring third parties and not remediating known gaps timely.

The identified security management control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- SOC 1 reports were not monitored and reviewed to assess CUECs, including validation of whether management’s internal controls relevant to the CUECs, are designed, implemented and operating effectively.
- Management internal control procedures did not identify financially significant risks, establish and implement controls, track known risk exposure and remediate control gaps.

### IT Operations Controls

Effective IT operations controls support the reliability of various aspects of operating the IT environment related to the complete and accurate processing of transactions and the protection of information used in that processing. IT operations involves computer job management tasks related to scheduling and running jobs (programs), monitoring the successful completion of those jobs, and detecting and addressing job failures timely. Relevant jobs may accept, process, and move data from one IT application to another via system interfaces for inclusion in financial reporting. IT administrators may also utilize programs or software that supports maintenance of the IT environment or data, including tasks responsible for backing up financially relevant programs and data.

The identified IT operations weaknesses in aggregate represent a significant risk to the DLA financial statements, IT environment, and financial applications. Absent or ineffective controls around IT operations increases the risk that issues with programs that are not scheduled correctly or don't process to completion, may not be addressed, or may be addressed inappropriately, and hardware or software issues will result in the loss of financially relevant data or the ability to accurately process that data.

The identified IT operations control weaknesses that represent a significant risk to the DLA financial management information systems environment include the following:

- Contingency planning (CP) processes and controls failed in allowing management to backup system data.

***Recommendations***

Implement controls to address deficiencies in access controls, configuration management, segregation of duties, security management procedures and IT operations to include:

### Access Controls

- Restrict access to authorized users in accordance with the least privilege principle. Review and approve all access, including justification of business needs.
- Routinely monitor and revalidate access needs for business users, privileged users and terminated and inactive users.
- Monitor user activity, identify and audit security violations and assess privileged and sensitive users and transactions.

**Configuration Management Controls**

- Review, approve and test changes prior to implementation, to include user testing and functionality assessments.
- Monitor source code, configurations and production environments for unauthorized changes.
- Segregate conflicting roles between development and production environments.

**Segregation of Duties Controls**

- Identify, periodically review and document sensitive and conflicting roles, enforce established segregation of duties processes, and assess conflicts during account provisioning and management. Segregate conflicting roles where possible, and if unavoidable, document business rationale and monitor user activity.

**Security Management/Governance Over Implementation of Security Controls**

- Establish a process to evaluate and incorporate service provider reports, findings, and controls into management's security documentation, governance process, and application control environment.
- Document risks and controls in place, identify gaps, and complete corrective actions to strengthen the internal control environment. Improve documentation, test and validate controls, and remediate findings.

**IT Operations Controls**

- Design and implement controls to periodically backup and monitor system data to successfully respond to incidents and prevent the permanent loss of data.

**Appendix B – Significant Deficiencies**

**I. Revenue**

Revenue arises when DLA sells goods to the public. The amounts of these transactions make it critical for DLA to properly record and reconcile these transactions to ensure timely, appropriate recognition of costs to the end users. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls that provide reasonable assurance that revenues applicable to the agency's operations are properly recorded and accounted for to permit the preparation of reliable financial reports and maintain accountability of assets.

A. **Improper Revenue Recognition in Accordance with Accounting Standards.** DLA lacked policies, procedures and controls to properly document and review relevant facts and apply the appropriate revenue accounting under SFFAS No. 7, *Accounting for Revenue and Other*

*Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, which impacted the revenue and gross cost accounts on the statements of net cost.

***Recommendations***

Consider the following corrective actions related to the conditions described above:

A. **Improper Revenue Recognition in Accordance with Accounting Standards.** Design and implement revenue recognition policies, procedures and controls in accordance with SFFAS No. 7. The policies should include considering the appropriate relevant facts to determine that revenue and costs of goods sold are properly recorded and presented in the financial statements. and ensure that sales are subject to a sufficient level of management review.

## II. Environmental Liabilities

ELs are comprised of cleanup costs associated with the restoration of sites on real property that DLA manages. In accordance with FMFIA, management is responsible for establishing and maintaining internal controls to achieve reliable financial reporting. However, we identified deficiencies in controls listed below, which, when aggregated, we consider to be a significant deficiency.

A. **Inadequate Controls Over Estimation Processes.** DLA did not have effectively designed management review controls to evaluate the completeness and measurement of the EL and the EL recorded in the financial statements. There was a lack of sufficient evidence of management's review, including management's review of the completeness and accuracy of the information used in the valuation of the EL.

***Recommendations***

Consider the following corrective actions related to the deficiencies identified above:

A. **Inadequate Controls Over Estimation Processes.** Design and implement formalized management review controls that adequately document management's review of the EL, including establishing a thresholds for review, documentation of findings and actions taken by management.

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# Report of Independent Auditors on Compliance and Other Matters Based on an Engagement to Audit the Financial Statements Performed in Accordance with *Government Auditing Standards*

The Director of the Defense Logistics Agency and the
Inspector General of the Department of Defense

We were engaged to audit, in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States (*Government Auditing Standards)* and the provisions of Office of Management and Budget (OMB) Bulletin No. 24-01, *Audit Requirements for Federal Financial Statements,* the financial statements of the National Defense Stockpile Transaction Fund of the Defense Logistics Agency (DLA), which comprise the balance sheet as of September 30, 2023, and the related statements of net cost and changes in net position and statement of budgetary resources for the year then ended, and the related notes (collectively referred to as the "financial statements"), and have issued our report thereon dated November 8, 2023. Our report disclaims an opinion on the financial statements because DLA continues to have unresolved accounting issues and material weaknesses in internal controls that cause DLA to be unable to provide sufficient evidential support for complete and accurate financial statements on a timely basis.

**Report on Compliance and Other Matters**

In connection with our engagement to audit the financial statements, we performed tests of DLA's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the financial statements, as well as the requirements referred to in the Federal Financial Management Improvement Act of 1996 (FFMIA). However, providing an opinion on compliance with those provisions was not an objective of our engagement, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and the provisions of OMB Bulletin No. 24-01, as described below. Additionally, if the scope of our work had been sufficient to enable us to express an opinion on the financial statements, other instances of noncompliance or other matters may have been identified and reported herein.

Our Report on Internal Control Over Financial Reporting dated November 8, 2023, includes additional information related to the financial management systems and internal controls that were found not to comply with the requirements, relevant facts pertaining to the noncompliance, and our recommendations to the specific issues presented.

As referenced in the Fiscal Year (FY) 2023 DLA Statement of Assurance, DLA provides no assurance that the internal controls over operations, financial systems, reporting and compliance are operating effectively in compliance with the Federal Managers' Financial Integrity Act (FMFIA), Section 4; FFMIA of 1996, Section 803; and *Management's Responsibility for Enterprise Risk Management and Internal Control,* OMB Circular No. A-123 Appendix D.

**FFMIA**

Under FFMIA, we are required to report whether DLA's financial management systems substantially comply with federal financial management system requirements, applicable federal accounting standards, and the United States Standard General Ledger (USSGL) at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements. The results of the tests disclosed instances in which DLA's financial management systems did not substantially comply with federal financial management system requirements, applicable federal accounting standards or the USSGL.

(a) Federal financial management system requirements

EY identified as part of the Financial Information Systems material weakness, contained in the Report on Internal Control Over Financial Reporting, noncompliance with federal financial management system requirements for multiple systems. Weaknesses identified include those associated with user access, configuration management/change controls, segregation of duties, security management and IT operations. These financial system deficiencies prevent DLA from being compliant with federal financial management system requirements and inhibit DLA's ability to prepare complete and accurate financial reporting.

(b) Noncompliance with applicable federal accounting standards

As referenced in Note 1 to the financial statements, DLA self-identified that the design of their financial and nonfinancial systems does not allow DLA to comply with applicable federal accounting standards, including not being able to collect and record financial information as required by U.S. generally accepted accounting principles. EY also identified noncompliance with federal accounting standards during our testing, which was included in our Report on Internal Control Over Financial Reporting.

(c) Noncompliance with USSGL posting logic at the transaction level

EY also identified noncompliance with USSGL posting logic during our testing, which was included in our Report on Internal Control Over Financial Reporting.

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**FMFIA**

Federal Managers' Financial Integrity Act (FMFIA) of 1982 requires federal entities to establish internal controls, perform ongoing evaluations of the adequacy of the entity's system of internal control, and prepare related reports. The Government Accountability Office's (GAO's) *Standards for Internal Control in the Federal Government* (commonly referred to as the "GAO Green Book") issued under the authority of FMFIA, establishes five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communication and Monitoring. To determine if an entity's internal control system is effective, the Green Book requires management to assess the design, implementation and operating effectiveness of the five components of the entity's internal control system.

DLA has not implemented a formal internal control program that would allow it to substantially comply with FMFIA and the related GAO Green Book requirements, leading to inadequate control environment, risk assessment and monitoring processes.

DLA was not able to provide evidence that they are in compliance with significant aspects of OMB Circular A-123, which implemented FMFIA. DLA provided a FY 2023 Statement of Assurance, however there was not sufficient evidence that DLA fully completed an organizational risk assessment, identified relevant risks related to the financial statement assertions, documented the internal control standards as it relates to those assertions, performed internal control testing, and reported and tracked control deficiencies at the control level for each process identified. DLA provided evidence demonstrating that DLA has started to implement a testing strategy, however, DLA is unable to provide evidence that the extent of testing and review performed is sufficient to meet the requirements of FMFIA.

**Anti-Deficiency Act (ADA)**

The Anti-Deficiency Act (ADA) Title 31 U.S.C. Section 1341 prohibits federal employees from obligating funds in excess of an appropriation or before funds are available, and from accepting unauthorized voluntary services. As required by Federal Law (OMB A-11 Section 120), an apportionment is an OMB-approved plan to use budgetary resources that is legally binding. Any obligations and expenditures (disbursements) that exceed an apportionment are a violation of, and are subject to reporting under, the ADA.

During FY 2023, DLA identified that it may have a potential ADA violation related to obligations incurred against a multi-year appropriation prior to OMB apportionment. This matter remains under formal investigation to determine if an ADA violation occurred.

***DLA's Response to Findings***

*Government Auditing Standards* require the auditor to perform limited procedures on DLA's response to the findings identified in our engagement to audit and described in the accompanying Management's Response to the Audit Reports dated November 8, 2023. DLA's response was not subjected to the other auditing procedures applied in the engagement to audit the financial statements and, accordingly, we express no opinion on the response.

***Purpose of This Report***

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on the entity's compliance. This report is an integral part of an engagement to perform an audit in accordance with *Government Auditing Standards* in considering the entity's compliance. Accordingly, this communication is not suitable for any other purpose.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2023 on our consideration of DLA's internal control over financial reporting. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and the results of that testing, and not to provide an opinion on the effectiveness of DLA's internal control over financial reporting. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DLA's internal control over financial reporting.

Ernst + Young LLP

November 8, 2023

# Management's Response to Audit Reports

**DEFENSE LOGISTICS AGENCY**
**HEADQUARTERS**
**8725 JOHN J. KINGMAN ROAD**
**FORT BELVOIR, VIRGINIA 22060-6221**

MEMORANDUM FOR DEPARTMENT OF DEFENSE OFFICE OF THE INSPECTOR GENERAL

SUBJECT: Fiscal Year 2023 Financial Statement Audit

Thank you for the opportunity to comment on Ernst & Young, LLP's Independent Auditor Reports on the Defense Logistics Agency's (DLA) Fiscal Year (FY) 2023 financial statements. DLA remains fully committed to remediating audit findings, improving the accuracy of our financial data and reporting, and making progress towards unmodified audit opinions.

We continue to review audit findings from prior and current financial statement audits and are focused on remediating material weaknesses identified in Ernst & Young, LLP's Report on Internal Control over Financial Reporting. DLA will prioritize Agency requirements to address the scope limitations and align critical milestones within our Audit Roadmaps.

We appreciate Ernst & Young LLP due diligence during the FY 2023 audit. DLA reaffirms our commitment to achieving our audit goals within the Department in support of the Warfighter Always!

Susan J. Goodyear
Director, DLA Finance
Chief Financial Officer

# Introduction to the DLA NDSTF Principal Financial Statements

The DLA NDSTF principal financial statements and the accompanying notes (financial statements) included in this report are prepared pursuant to the requirements of the CFO Act of 1990 (Pub. L. 101-576) and expanded by GMRA (Pub. L. 103-356) and other applicable legislation. Other reporting requirements include the OMB Circular A-136, as amended. The responsibility for the integrity of the financial information included in these financial statements rests with the management of DLA NDSTF. The IPA was engaged to perform the audit of DLA NDSTF's financial statements and disclaimed an opinion on these financial statements. The Audit Report, and Management's Response to the Audit Report, accompany the unaudited financial statements.

### The DLA NDSTF financial statements consist of the following:

**The Balance Sheets** present those resources owned or managed by DLA NDSTF that represent future economic benefits (assets), amounts owed by DLA NDSTF that will require payments from those resources or future resources (liabilities), and residual amounts retained by DLA NDSTF comprising the difference (net position) as of September 30, 2023 and 2022.

**The Statements of Net Cost** present the net cost of DLA NDSTF operations for the years ended September 30, 2023 and 2022. DLA NDSTF's net cost of operations is the gross cost incurred by DLA NDSTF activities, less any exchange revenue earned and inter-entity eliminations from DLA NDSTF activities.

**The Statements of Changes in Net Position** present the change in DLA NDSTF's net position resulting from the net cost of DLA NDSTF's operations, budgetary financing sources, and other financing sources for the years ended September 30, 2023 and 2022.

**The Statements of Budgetary Resources** present how and in what amounts budgetary resources were made available to DLA NDSTF, the status of these resources, and the net outlays of budgetary resources for the years ended September 30, 2023 and 2022.

**The Notes to the Principal Financial Statements** provide detail and clarification for amounts in the principal financial statements.

**DLA Distribution Hosts the DDXX Academy**
DLA Distribution Expeditionary reservists set the flooring for an Alaskan Shelter during the DLA Distribution Expeditionary Academy on April 19, at DLA Distribution San Joaquin. **Photo By:** Julian Temblador

# Balance Sheets

As of September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 |
|---|---|---|
| **ASSETS** | | |
| **Intragovernmental** | | |
| Fund Balance with Treasury (Note 2) | $ 579,802 | $ 500,627 |
| Advances and Prepayments | 24,315 | - |
| **Total Intragovernmental** | **604,117** | **500,627** |
| **Other than Intragovernmental** | | |
| Cash and Other Monetary Assets | 5 | - |
| Accounts Receivable | 10 | 34 |
| Inventory and Related Property, Net (Note 3) | 384,642 | 762,581 |
| General Property, Plant and Equipment, Net (Note 4) | 352 | 574 |
| Advances and Prepayments | 1,238 | 1,460 |
| **Total Other than Intragovernmental** | **386,247** | **764,649** |
| **TOTAL ASSETS** | **$ 990,364** | **$ 1,265,276** |
| | | |
| **LIABILITIES (Note 5)** | | |
| **Intragovernmental** | | |
| Accounts Payable | $ 586 | $ 790 |
| Federal Employee Benefits Payable (Note 6) | 233 | 234 |
| **Total Intragovernmental** | **819** | **1,024** |
| **Total Other than Intragovernmental** | | |
| Accounts Payable | 249 | 715 |
| Environmental and Disposal Liabilities (Note 7) | 11,707 | 12,181 |
| Federal Employee Benefits Payable (Note 6) | 2,455 | 2,050 |
| Advances from Others and Deferred Revenue | - | 644 |
| Other Liabilities (Note 8) | 285 | 366 |
| **Total Other than Intragovernmental** | **14,696** | **15,956** |
| **TOTAL LIABILITIES** | **15,515** | **16,980** |
| | | |
| **Commitments and Contingencies (Note 9)** | | |
| | | |
| **NET POSITION** | | |
| Unexpended Appropriations - Funds from Other than Dedicated Collections | $ 236,551 | $ 125,000 |
| Cumulative Results of Operations - Funds from Other than Dedicated Collections | 738,298 | 1,123,296 |
| **TOTAL NET POSITION** | **974,849** | **1,248,296** |
| **TOTAL LIABILITIES AND NET POSITION** | **$ 990,364** | **$ 1,265,276** |

*The accompanying notes are an integral part of these statements.*

# Statements of Net Cost

For the Years Ended September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 |
|---|---|---|
| **Operations, Readiness & Support** | | |
| Gross Cost | $ 577,891 | $ 89,973 |
| Less: Earned Revenue | (190,256) | (101,704) |
| **Net Cost** | **387,635** | **(11,731)** |
| **NET COST OF OPERATIONS** | **$ 387,635** | **$ (11,731)** |

*The accompanying notes are an integral part of these statements.*

**Reassembly Ready**

Navy Seaman QI Zhu reassembles a nose landing-gear strut aboard the USS George H.W. Bush in the Adriatic Sea, Dec. 15, 2022.

**Photo By:** Navy Seaman Curtis Burdick

# Statements of Changes in Net Position

For the Years Ended September 30, 2023 and 2022 (dollars in thousands)

| | Unaudited FY 2023 | Unaudited FY 2022 |
|---|---|---|
| **Unexpended Appropriations** | | |
| Beginning Balances | $ 125,000 | $ - |
| Appropriations Received | 93,500 | 125,000 |
| Appropriations Transferred In/Out | 20,000 | - |
| Appropriations Used | (1,949) | - |
| **Net Change in Unexpended Appropriations** | **111,551** | **125,000** |
| **Total Unexpended Appropriations: Ending** | **$ 236,551** | **$ 125,000** |
| **Cumulative Results of Operations** | | |
| Beginning Balance | $ 1,123,296 | $ 1,111,062 |
| Appropriations Used | 1,949 | - |
| Imputed Financing | 688 | 503 |
| **Net Cost of Operations** | **387,635** | **(11,731)** |
| **Net Change in Cumulative Results of Operations** | **(384,998)** | **12,234** |
| **Cumulative Results of Operations: Ending Balance** | **738,298** | **1,123,296** |
| **TOTAL NET POSITION** | **$ 974,849** | **$ 1,248,296** |

*The accompanying notes are an integral part of these statements.*

### IG Conducts Fuel Spill Exercise

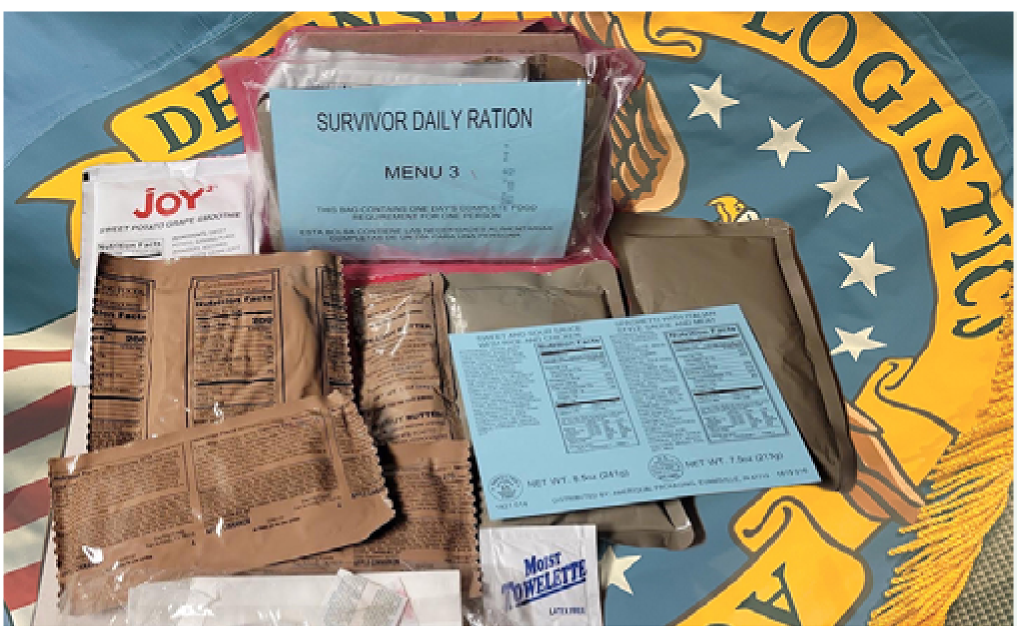
Members of the 56th Fighter Wing base response agencies participate in a Defense Logistics Agency fuel spill exercise May 4, 2023, at Luke Air Force Base, Arizona. The exercise was to test the response operations of base recovery agencies in the event of a hazardous fuel spill emergency to ensure installation safety and minimal environmental impact. **Photo By:** Airman 1st Class Katelynn Jackson

# Combined Statements of Budgetary Resources

For the Years Ended September 30, 2023 and 2022 (dollars in thousands)

| | | Unaudited FY 2023 | | Unaudited FY 2022 |
|---|---|---|---|---|
| **BUDGETARY RESOURCES** | | | | |
| Unobligated Balance from Prior Year Budget Authority, Net | $ | 430,184 | $ | 263,408 |
| Appropriations | | 113,500 | | 125,000 |
| Spending Authority from Offsetting Collections | | 42,077 | | 94,582 |
| **TOTAL BUDGETARY RESOURCES** | **$** | **585,761** | **$** | **482,990** |
| **STATUS OF BUDGETARY RESOURCES** | | | | |
| New Obligations and Upward Adjustments | $ | 131,520 | $ | 54,649 |
| Unobligated Balance, End of Year: | | | | |
| Apportioned, Unexpired Accounts | | 196,826 | | 166,499 |
| Unapportioned, Unexpired Accounts | | 257,415 | | 261,842 |
| **Unexpired Unobligated Balance, End of Year** | | **454,241** | | **428,341** |
| **Total Unobligated Balance, End of Year** | | **454,241** | | **428,341** |
| **TOTAL BUDGETARY RESOURCES** | **$** | **585,761** | **$** | **482,990** |
| **OUTLAYS, NET** | | | | |
| Outlays, Net | $ | 34,325 | $ | (61,994) |
| **AGENCY OUTLAYS, NET** | **$** | **34,325** | **$** | **(61,994)** |

*The accompanying notes are an integral part of these statements.*




**DLA Troop Support Survivor Daily Ration (SDR)**
SDRs are currently comprised of 10 unique entrees configured to fit a full day's worth of food for an adult in a single package. They also have a minimum shelf life of three years at 80 degrees Fahrenheit. **Photo By:** Michael Hong

# Notes to the Principal Financial Statements (Unaudited)

## Note 1: Summary of Significant Accounting Policies (Unaudited)

### A. Reporting Entity

Created in 1961, DLA is a component of the U.S. DoD and reports to the OUSD for Acquisition and Sustainment through the Assistant Secretary of Defense for Sustainment. DLA provides material and services to components of DoD (including the U.S. Army, Navy, Air Force, Marine Corps and Space Force), other Federal agencies, and public entities. DLA accomplishes its mission and goals through the operations of the DLA WCF, DLA GF, and DLA NDSTF. These financial statements and accompanying notes herein only refer to the activities of DLA NDSTF.

Initially authorized by the Strategic and Critical Materials Stock Piling Act of 1946, the NDS (commonly known as DLA NDSTF) is a physical reserve of definite quantities of S&C materials, owned by the U.S. government, authorized for use during times of National Emergencies. Executive Order 12626, issued February 25, 1988, designated the Secretary of Defense as the NDS Manager. The Secretary of Defense delegated the management responsibilities to the OUSD for Acquisition and Sustainment through the Assistant Secretary of Defense for Sustainment. The operational activities of the NDS are delegated to the Director of DLA.

The DLA SM program is a distinct revolving fund which operates under the authority of the Strategic and Critical Materials Stock Piling Act (50 U.S.C.) §98, et seq. Under the Act, critical materials are stockpiled in the interest of National Defense to preclude a dangerous and/or costly dependence upon foreign or single source suppliers. The NDS Manager administers the acquisition, storage, management, and disposal of the stockpile. The NDAA authorized the NDS Manager to acquire materials determined to be strategic and critical to meet defense, industrial, and essential civilian needs of the U.S. The legislation further provided authority to dispose of certain materials, with proceeds deposited in the fund to finance future stockpile operating costs and procurement of replenishment materials

### B. Basis of Presentation and Accounting

**Basis of Presentation and Accounting:** The DLA NDSTF fiscal year ends September 30. The accompanying financial statements account for all resources for which DLA NDSTF is responsible. These financial statements present the financial position, results of operations, changes in net position, and budgetary resources of DLA NDSTF, as required by the CFO Act of 1990, expanded by the GMRA of 1994, and other applicable legislation. The financial statements are prepared from the books and records of DLA NDSTF, in accordance with U.S. GAAP, promulgated by the FASAB[14], and presented in the format prescribed by the OMB Circular A-136, except as identified in Note 1.C., *Departures from U.S. GAAP*, and in the following paragraphs.

The DLA NDSTF financial statements reflect both accrual and budgetary accounting transactions, except as identified in Note 1.C., *Departures from U.S. GAAP*. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when incurred, without regard to the receipt or payment of cash. Budgetary accounting is based on concepts set forth by OMB Circular A-11, *Preparation, Submission, and Execution of the Budget*, as amended, which provides instructions on budget execution. Budgetary accounting is designed to recognize the budgetary resources and the related status of those budgetary resources, including the obligation and outlay of funds according to legal requirements, which in many cases is made prior to the occurrence of an accrual-based transaction. Budgetary accounting is essential for compliance with legal constraints and controls over the use of Federal funds.

[14] FASAB is the official body for setting accounting standards of the U.S. government.

The DLA NDSTF is unable to fully prepare financial statements in conformity with and implement all elements of U.S. GAAP (refer to Note 1.C., *Departures from U.S. GAAP*), the form and content requirements for Federal government entities specified by OMB Circular A-136, due to limitations of financial and nonfinancial management processes and systems that support the financial statements. In addition, the financial management systems used by DLA NDSTF are unable to meet all full accrual and budgetary accounting requirements as many of the financial and nonfinancial feeder systems and processes were not designed to collect and record financial information on the full accrual accounting basis as required by U.S. GAAP. These systems were designed to support reporting requirements for maintaining accountability over assets, reporting the status of Federal appropriations, and recording information on a budgetary basis, rather than preparing financial statements in accordance with U.S. GAAP.

Therefore, DLA NDSTF is continuing the necessary actions required to bring its financial and nonfinancial systems and processes to generate financial statements and the accompanying notes in accordance with U.S. GAAP and in compliance with the reporting requirements of OMB Circular A-136. DLA is assessing financial feeder systems and processes and their conformance to existence, completeness, and accuracy requirements as required by U.S. GAAP and OMB Circular A-136. As DLA NDSTF identifies non-conforming data issues, the Agency will continue to implement interim mitigation processes to address these limitations. In addition, DLA NDSTF is remediating material weaknesses found in all end-to-end business process cycles pertaining to reconciliations and adequacy of the supporting documentation identified through audits and other compliance reporting.

**Statements of Budgetary Resources:** The budgetary accounting concepts are recognized in the Statements of Budgetary Resources. The Statements of Budgetary Resources present: (1) budgetary resources for the fiscal year; (2) status of those budgetary resources (includes obligated[15] amounts and unobligated[16] amounts for the fiscal year); and (3) Outlays[17], Net for the fiscal year, which is comprised of Outlays less Offsetting Receipts (cash transactions). DLA NDSTF's budgetary resources[18] include unobligated balances of resources from prior years and new resources, consisting of spending authority from offsetting collections and appropriations.

## Intragovernmental and Other than Intragovernmental Transactions:

SFFAS 1, *Accounting for Selected Assets and Liabilities*, distinguishes between Intragovernmental and Other than Intragovernmental assets and liabilities. Intragovernmental assets and liabilities arise from transactions among Federal entities. Intragovernmental assets are claims other Federal entities owe to DLA NDSTF. Intragovernmental liabilities are claims DLA NDSTF owes to other Federal entities, whereas Other than Intragovernmental assets and liabilities arise from transactions with public entities. The term "public entities" encompasses domestic and foreign persons and organizations outside the U.S. Government. Other than Intragovernmental assets are claims of DLA NDSTF against public entities. Other than Intragovernmental liabilities are amounts that DLA NDSTF owes to public entities.

The DLA NDSTF engages in transactions with other DoD and Federal entities that generate inter-DoD and intragovernmental balances; however, DLA NDSTF is unable to reconcile and resolve differences between balances and transactions with other DoD and Federal entities in accordance with OMB Circular A-136 requirements and TFM, Volume I, Part 2, Chapter 4700, *Federal Entity Reporting Requirements for the Financial Report of the United States Government*.

The process is not fully implemented (refer to Note 1.C., *Departures from U.S. GAAP*, related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions).

**Intra-departmental Transactions:** DLA NDSTF is ultimately responsible for the accuracy of its trading partner data and initiating actions to reconcile balances with its

[15] Per OMB Circular A-11, Section 20, "Obligated amount means a legally binding agreement that will result in outlays, immediately or in the future."

[16] Per OMB Circular A-11, Section 20, "Unobligated amount means the cumulative amount of budget authority that remains available for obligation under law in unexpired accounts.

[17] Per OMB Circular A-11, Section 20, "Outlay means a payment to liquidate an obligation (other than the repayment to the Treasury of debt principal)... Outlays are a measure of Government spending."

[18] Per OMB Circular A-11, Section 20, "Budgetary resources are amounts available to incur obligations in a given year. Budgetary resources consist of new budget authority and unobligated balances of budget authority provided in previous years."

trading partners; however, DLA NDSTF is unable to resolve the reconciling differences in amounts reported for the buyer/ seller transactions reciprocal category with Other ODOs, (refer to Note 1.C., *Departures from U.S. GAAP* related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions). A DoD reporting entity unable to provide detail transactions at the appropriate time of the financial statement reporting cycle must adjust its balance to match the seller's or buyer's supportable data.

**Classified Activities:** Accounting standards require all reporting entities to disclose that accounting standards allow certain presentations and disclosures to be modified, if needed, to prevent the disclosure of classified information.

**Use of Estimates:** The DLA NDSTF management has made certain estimates and assumptions when reporting assets, liabilities and expenses and disclosures in the notes. DLA NDSTF's estimates are based on historical experience, current events and other assumptions that are believed to be reasonable under the circumstances. However, uncertainties associated with these estimates exist and actual results may differ from these estimates. Significant estimates reported in the financial statements include: (1) environmental and disposal liabilities and (2) FECA actuarial liability as of the date of these financial statements.

## C. Departures from U.S. GAAP

Financial management systems and operations continue to be evaluated and modified as DLA NDSTF strives to remediate its material weaknesses and record and report its financial activity in accordance with U.S. GAAP. Therefore, DLA NDSTF is determining the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with U.S. GAAP. However, due to the financial management systems and operational limitations, the known departures from U.S. GAAP described below have been identified that impact DLA NDSTF financial statements although other departures from U.S. GAAP may exist that have not been identified.

**Definition of Reporting Entity (Note 1.A.):** The DLA NDSTF has not completed analyzing material applicable business relationships with other organizations to identify consolidation entities, disclosure entities, or related parties in accordance with SFFAS 47, *Reporting Entity* (effective FY2018). As a result, DLA NDSTF is unable to determine if there are consolidation entities that are required to be consolidated and disclosed in DLA NDSTF financial statements or disclosure entities and related parties where the nature and magnitude of such relationships are required to be disclosed in a Disclosure Entities and Related Parties note to the financial statements.

**Statements of Net Cost:** The DLA NDSTF does not have policies and compliant processes in place to present its major program costs aligned with DLA NDSTF mission and goals by responsibility segments in accordance with SFFAS 4, *Managerial Cost Accounting Concepts and Standards*, and OMB Circular A-136.

**Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions (Note 1.B., Note 10, and Note 11):** The DLA NDSTF does not have compliant processes in place to properly report and distinguish between intragovernmental, intra-departmental, and Other than Intragovernmental transactions in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*.

**Inter-Entity Cost (Note 1.S.):** The DLA NDSTF does not have compliant processes in place to recognize all significant inter-entity costs related to inputs of its goods or services provided to entities for a fee or user charge in accordance with SFFAS 55, *Amending Inter-Entity Cost Provisions*, (effective FY 2019). Generally, the fees and user charges should recover the full costs of those goods and services. Thus, the cost of inter-entity goods or services needs to be recognized by the receiving entity in order to determine fees or user charges for goods and services sold.

**Fund Balance with Treasury (Note 1.F. and Note 2):** The DLA NDSTF is not able to account for FBwT in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, due to its inability to identify and reconcile beginning balances and unknown entity transactions in DoD SoD to determine if they impact NDSTF FBwT balances.

**Accounts Receivable, Revenue, and Gains (Notes 1.G, 1.H., and 1.S.):** The DLA NDSTF does not have policies and compliant processes in place to recognize gains in accordance with SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. DLA NDSTF improperly recognized gains when: (1) acquiring purchased stockpile materials and receiving upgraded and/or reconditioned stockpile materials and (2) making adjustments to the value of its stockpile materials for which it did not have sufficient evidential matter to support the historical cost in accordance with SFFAS 3 (refer to Note 1.C., *Departures from U.S. GAAP,* related to Inventory and Related Property, Net).

**Inventory and Related Property, Net (Note 1.H. and Note 3):** The DLA NDSTF does not have policies and compliant processes in place to account for stockpile materials in accordance with SFFAS 3, *Accounting for Inventory and Related Property*, and SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. Furthermore, DLA NDSTF has not completed establishing beginning balances for stockpile materials using deemed cost and has not made an unreserved assertion as permitted by SFFAS 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials* (effective FY 2017). More specifically:

Inventory Quantities: The DLA NDSTF does not have proper policies and procedures to record inventory quantities in the proper period and to sufficiently support the existence and completeness of the inventory quantities recorded;

Stockpile Materials Acquisition: The DLA NDSTF's accounting system does not properly account for stockpile material acquisitions due to system limitations. For acquisitions of stockpile materials, DLA NDSTF recognized a gain when purchased stockpile materials were received. DLA NDSTF also recognized an expense when approving the invoice for purchased stockpile materials. The cost of purchased stockpile materials should not be reported as an expense at the point the stockpile material is purchased, but rather when stockpile material is issued for use or sale. The results are an overstatement to total gross cost and total earned revenue reported in the Statements of Net Cost, however the net impact of the overstatements offset each other in Total Net Cost of Operations;

Stockpile Materials Upgraded and/or Reconditioned: The DLA NDSTF does not properly account for stockpile material upgraded and/or reconditioned transactions. The outbound and inbound movements of stockpile material during the stockpile material upgraded and/or reconditioned process does not meet the criteria for expense and revenue recognition. DLA NDSTF recognized a loss when the stockpile materials were provided to a third-party entity for upgrade and/or reconditioning. When the stockpile materials were returned, DLA NDSTF recognized a gain. The results are an overstatement to total gross cost and total earned revenue reported in the Statements of Net Cost; and

Stockpile Materials Valuation: The DLA NDSTF does not have proper policies and procedures over the inventory valuation process. During 2023, DLA NDSTF made deemed cost adjustments to the value of its stockpile materials for which it did not have sufficient evidential matter to support the historical cost in accordance with SFFAS 3. The adjustments recognized a gain or a loss for each inventory item. These adjustments were not made in accordance with U.S. GAAP. The results are an overstatement to total gross cost and total earned revenue reported in the Statements of Net Cost and a misstatement to Inventory and Related Property, Net reported in the Balance Sheet as of September 30, 2023.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Advances and Prepayments; Accounts Receivable, Revenue, and Gains; and Accounts Payable, Expenses, and Undelivered Orders.)

**Advances and Prepayments (Note 1.K. and Note 1.M.):** The DLA NDSTF does not have compliant processes in place to properly report Advances and Prepayments in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities* (refer to Note 1.C., *Departures from U.S. GAAP*, related to Inventory and Related Property, Net.)

**Accounts Payable, Expenses, and Undelivered Orders (Notes 1.M. and 1.T.; Note 3; Note 5; Note 6; and Note 10):**

The DLA NDSTF does not have policies and compliant processes in place to account for accounts payable, expense accruals, and the related UDO's in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, and SFFAS 5, *Accounting for Liabilities of the Federal Government*. More specifically:

Negative Payable: The DLA NDSTF processes allow for payment to be made prior to the goods receipts being posted in the accounting system. Given that DLA does not post goods receipts timely, and that the posting of goods receipts triggers the recognition of expense and accounts payable, these processes result in negative balances existing in accounts payable (refer to Note 1.C., *Departures from U.S. GAAP*, related to Inventory and Related Property, Net);

**Expenses:** The DLA NDSTF improperly recognized expenses when: (1) acquiring stockpile materials; (2) receiving upgraded and/or reconditioned stockpile materials; and (3) adjusting the value of its stockpile materials, resulting in the improper recognition of losses and an overstatement of expenses. In addition, DLA is unable to support historical costs; therefore, cost of goods sold is not properly recognized (refer to Note 1.C., *Departures from U.S. GAAP*, related to Inventory and Related Property, Net); and

**Undelivered Orders:** The DLA NDSTF does not have sufficient policies and procedures in place to record obligations at the time contracts are awarded in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*. In addition, DLA NDSTF is unable to support the UDO balance in the accounting system.

**Environmental and Disposal Liabilities (Notes 1.L. and 1.N.; and Note 7; and Note 9):** The DLA NDSTF does not have policies and compliant processes in place to reconcile asset listings to the amounts recorded for E&DL related to cleanup, asset closure, and asbestos associated with general PP&E, in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*; SFFAS 6, *Accounting for Property, Plant, and Equipment*, and Federal Financial Accounting and Auditing Technical Release 2, *Determining Probable and Reasonably Estimable for Environmental Liabilities in the Federal Government* (refer to Note 1.C., *Departures from U.S. GAAP*, related to Commitments and Contingencies).

**Commitments and Contingencies (Notes 1.L. and 1.N.; and Note 7; and Note 9):** The DLA NDSTF did not complete its assessment of commitments and contingencies in accordance with SFFAS 5, *Accounting for Liabilities of The Federal Government*, and SFFAS 12, *Recognition of Contingent Liabilities Arising from Litigation*: An Amendment of SFFAS 5, *Accounting for Liabilities of the Federal Government. Government* (refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities).

**Reconciliation of Net Cost to Net Outlays (Note 11):** The DLA NDSTF does not have an established policy for the reconciliation of net cost to net outlays in accordance with SFFAS 53, *Budget and Accrual Reconciliation*. DLA NDSTF is also unable to fully prepare the reconciliation of net cost to net outlays in conformity with U.S. GAAP due to limitations of financial and nonfinancial management processes and systems that support the underlying financial information (refer to Note 1.B., *Basis of Presentation and Accounting*).

**Public-Private Partnerships:** The DLA NDSTF has not completed analyzing all applicable business relationships to determine if these arrangements or transactions indicate the existence of Public-Private Partnership (P3) relationships, risk-sharing arrangements or transactions lasting more than five years between public and private sector entities, in accordance with SFFAS 49, *Public-Private Partnerships: Disclosure Requirements*, (effective FY 2019). As a result, DLA NDSTF is unable to determine the nature of such partnerships and related Federal funding amounts required to be disclosed in a P3 note to the financial statements, if applicable.


**DLA Surplus Helping Lower Veteran Homelessness Rates**

Veteran homelessness has dropped 55% since 2010, according to the U.S. Department of Housing and Urban Development. Veterans Affairs social workers and outreach specialists point to events like annual veterans stand downs, and the millions of dollars in military surplus property received from the Defense Logistics Agency each year as effective tools to engage and assist at-risk veterans. **Photo By:** Jake Joy

## D. Pronouncements Recently Issued but Not Yet Effective

FASAB has issued the following pronouncements that may affect future financial presentation, as well as financial management practices and operations of DLA NDSTF upon implementation. DLA NDSTF has not completed the process of evaluating the effects of these pronouncements and is unable to determine the materiality of changes that these pronouncements will have on its financial position, results of operations, changes in net position, and budgetary activity.

| **FASAB Statement No** | SFFAS 54 | SFFAS 57 (paragraphs 3 – 8, 11, and 12) | SFFAS 60 | SFFAS 61 |
|---|---|---|---|---|
| **FASAB Standard** | Leases: An Amendment of SFFAS 5, *Accounting for Liabilities of the Federal Government*, and SFFAS 6, *Accounting of Property, Plant, and Equipment* | Omnibus Amendments FY 2019 | Omnibus Amendments FY 2021 | Omnibus Amendments FY 2023 |
| **Adoption Required in FY** | Deferred to FY 2024 | Effective FY 2024 | Effective FY 2024 | Effective FY 2024 |

SFFAS 54 revises the current Federal financial reporting standards for lease accounting and requires that Federal lessees recognize a lease liability and a leased asset at the commencement of the lease term, unless it meets any of the scope exclusions or the definition/criteria of short-term leases, or contracts or agreements that transfer ownership, or intragovernmental leases. SFFAS 57, *Omnibus Amendments 2019*, SFFAS 60, *Omnibus Amendments 2021: Leases-Related Topics,* and SFFAS 61, *Omnibus Amendments 2023: Leases-Related Topics II*, amend certain references to leases affected by SFFAS 54, as well as other minor changes in order to improve clarity of existing statements.

## E. Appropriations and Funding Sources

The DLA NDSTF receives annual apportionments of spending authority from offsetting collections from OUSD based on expected sales of materials that have been deemed excess to the needs of the stockpile. The proceeds from the sale of materials are DLA NDSTF's major source of authority used to fund operations. The funds in the revolving fund do not expire but remain available for the NDS subject to Congressional and OUSD approval as part of the annual apportionment process.

For the year ended September 30, 2022, DLA NDSTF received a direct appropriation in the amount of $125.0 million from Public Law 117–103, *Consolidated Appropriations Act, 2022*, for the acquisition and retention of certain stockpile materials. The appropriations will remain available until September 30, 2024.

For the year ended September 30, 2023, DLA NDSTF received a direct appropriation in the amount of $93.5 million from Public Law 117–328, *Consolidated Appropriations Act, 2023*, for activities pursuant to the Strategic and Critical Material Stock Piling Act (50 U.S.C. 98 et seq.). The appropriations will remain available until September 30, 2025.

## F. Fund Balance with Treasury

The DLA NDSTF does not maintain cash in a commercial bank, but rather in the U.S. Treasury. DLA NDSTF's FBwT includes the amount available for DLA NDSTF to pay current liabilities and finance authorized purchases, except as restricted by law. The disbursing offices of DFAS, the U.S. Army Corps of Engineers, GSA, and the Department of State's financial service centers process DLA NDSTF's cash collections, disbursements, and adjustments.

The DLA NDSTF is the only agency using Treasury Account Symbol (TAS) 97X4555, the National Defense Stockpile Transaction Fund, which allows DLA to identify the transactions belonging to this fund. On a monthly basis, DLA NDSTF adjusts its FBwT account balance to bring its cash balance in agreement with the U.S. Treasury cash balance reported on the CARS. The adjustments represent the undistributed disbursements and collections amounts that have been reported to Treasury but have not yet been posted to DLA NDSTF's accounting system. Undistributed amounts can be a result of timing, invalid line of accounting, invalid TAS information, and unsupported and unreconciled differences.

The DLA NDSTF's accounting service provider, DFAS, uses U.S. Treasury suspense accounts to hold transactions temporarily prior to identifying the correct appropriation. Suspense account items represent the amounts that are reported to U.S. Treasury at the TI Level (TI-17, TI-21, TI-57, TI-97), but have not yet been classified to a DLA NDSTF TAS. The transactions in suspense accounts include unidentified collections, disbursements, and Intragovernmental Payment and Collection transactions at month end. DFAS researches suspense transactions in each TI to post them against the appropriate line of accounting. The current balances for DLA NDSTF suspense transactions are derived from the DFAS suspense Account UoT.

U.S. Treasury also compares DoD's FBwT reported by DFAS with comparable data submitted by financial institutions and U.S. Treasury Regional Financial Centers and notifies DoD of differences in collection and disbursement data on the SOD report. DFAS reviews the SOD report to research and resolve differences. The current balances for DLA NDSTF SOD transactions are derived from DFAS management analysis and the SOD UoT.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Fund Balance with Treasury and Note 2, *Fund Balance with Treasury*.)

## G. Accounts Receivable

Accounts Receivable represents amounts due to DLA NDSTF from public sources. DLA's accounts receivable arise from sales of stockpile materials.

The DLA NDSTF customers remit payments in advance before material is shipped. There are instances when, the material delivered to the customer is in excess of the amount paid for in advance by the customer. When this occurs, DLA NDSTF establishes an accounts receivable for the amount of material delivered in excess of the advance payment received. These amounts are minimal and historically are collected within 30-60 days. The risk of uncollected receivable is minimal; therefore, DLA NDSTF does not establish an allowance for doubtful accounts.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable.)

## H. Inventory and Related Property, Net

The DLA NDSTF's Inventory and Related Property, Net includes stockpile materials, which are categorized as:

**Stockpile Materials Held for Sale:** Stockpile materials held for sale is comprised of materials deemed to be excess and have been identified for disposal based on the ASP.

**Stockpile Materials Held in Reserve for Future Use:** Stockpile materials held in reserve for future use is comprised of S&C materials held due to statutory requirements for use in National Defense, conservation, or National Emergencies. The S&C materials are not held with the intent of selling in the ordinary course of business.

Both stockpile materials classifications are valued at historical cost. They are recorded as assets when acquired and recorded as expenses when sold.

(Refer to Note 1.C., *Departures from U.S. GAAP,* related to Accounts Receivable, Revenue, and Gains, Accounts Payable, Expenses, and Undelivered Orders, and Inventory and Related Property, Net, and Note 3, *Inventory and Related Property, Net.*)

## I. General Property, Plant and Equipment, Net

The DLA NDSTF's PP&E consists of general equipment used to facilitate the Agency's mission. DLA NDSTF uses the Straight-Line (S/L) method to calculate and record depreciation expense. The S/L method is based on the acquisition cost and expensed over the asset's useful life in accordance with SFFAS 6, *Accounting for Property, Plant, and Equipment*.

**Capitalization Threshold:** The DLA NDSTF's General PP&E assets are recorded at the historical acquisition cost when an asset has a useful life of two or more years and when the acquisition cost equals or exceeds the $250,000 capitalization threshold.

The DLA NDSTF also capitalizes improvements added to existing General PP&E assets if the improvements equal or exceed the capitalization threshold, extend the useful life, or increase the size, efficiency, or capacity of the asset.

Depreciation Method and Useful Life:

| Asset Classes | Depreciation Method | Useful Life (Years) |
|---|---|---|
| General Equipment | S/L | 5 or 10 |

(Refer to Note 4, *General Property, Plant and Equipment, Net.*)

## J. Leases

As of September 30, 2023, the DLA NDSTF has 14 cancelable operating leases for real property such as land, warehouse storage facilities, and office space. All leases are executed with Federal agencies and have terms ranging from 5 to 10 years. In addition, DLA NDSTF leases include 13 occupancy agreements held with GSA. DLA is billed a cost based on the space DLA is occupying. DLA has the privilege to terminate the occupancy agreements based on the availability of funds or with four-months' notice. The other DLA NDSTF lease is with a DoD agency. DLA has the right to terminate the lease with 30 days' notice.

## K. Advances and Prepayments

Advances represent cash outlays to cover a part or all of the recipients' anticipated expenses or as advance payments for the cost of goods and services the entity acquires. Prepayments represent payments made by a federal entity to cover certain periodic expenses before those expenses are incurred.

When advances are permitted by law, legislative action, or presidential authorization, DLA's policy is to record advances or prepayments. DLA recognizes advance payments made for stockpile materials before the goods are provided by the contractor.

(Refer to Note 1.C., *Departures from U.S. GAAP,* related to Advances and Prepayments.)

## L. Commitments and Contingencies

In accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government,* as amended by SFFAS 12*, Recognition of Contingent Liabilities Arising from Litigation*, DLA NDSTF evaluates all contingent liabilities based on three criteria: probable, reasonably possible, and remote. DLA NDSTF recognizes contingent liabilities in DLA NDSTF's Balance Sheets and Statements of Net Cost when the loss is determined to be probable and reasonably estimable. DLA NDSTF discloses those contingencies that are reasonably possible. DLA NDSTF does not disclose or record contingent liabilities when the loss is considered remote.

The DLA NDSTF recognizes that the estimated liability may be a specific amount or a range of amounts. If an amount within the range is a better estimate than any other amount within the range, that amount is recorded. If no amount within the range is a better estimate than any other amount, the minimum amount of the range is recorded and the range and a description of the nature of the contingency are disclosed.

In the event of an adverse judgment against the Government, some of the liabilities may be payable from the U.S. Treasury. For legal contingency matters where DLA Counsel is unable to express an opinion regarding the likely outcome of the case and an estimate of the potential legal liability cannot be made, the total amount claimed against the government is classified as "Reasonably Possible" and disclosed if available.

The DLA NDSTF records an accrual for and discloses probable E&DL contingencies in Note 9, *Commitments and Contingencies*.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities and Commitments and Contingencies; Note 7, *Environmental and Disposal Liabilities.* and Note 9*, Commitments and Contingencies*.)

## M. Liabilities

Liabilities represent probable and measurable future outflows of resources as a result of past transactions or events and are recognized when incurred, regardless of whether there are budgetary resources available to pay the liabilities. However, liabilities cannot be liquidated without legislation providing resources and legal authority (refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders and Advances and Prepayments, Note 5, *Liabilities Not Covered by Budgetary Resources*, and Note 8, *Other Liabilities*.)

**Liabilities Covered and Not Covered by Budgetary Resources:** Liabilities covered by budgetary resources include those liabilities for which Congress appropriated funds and are otherwise available to pay amounts due as of the Balance Sheet dates. Liabilities not covered by budgetary resources are amounts owed in excess of available, congressionally appropriated funds and, therefore, no budgetary resources are available to pay amounts due as of the Balance

Sheet dates (refer to Note 5, L*iabilities Not Covered by Budgetary Resources*).

**Current and Noncurrent Liabilities:** The DLA NDSTF discloses its other liabilities between current and noncurrent liabilities in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*. The current liabilities represent liabilities that DLA NDSTF expects to settle within 12 months of the Balance Sheet dates. Noncurrent liabilities represent liabilities that DLA NDSTF does not expect to be settled within 12 months of the Balance Sheet dates (refer to Note 8, *Other Liabilities*).

**Accounts Payable:** Accounts Payable include amounts owed but not yet paid to Intragovernmental and Other than Intragovernmental entities for goods and services received by DLA NDSTF. DLA NDSTF estimates and records accruals when services are performed, or goods are received. DLA NDSTF also accrues liabilities incurred at month-end but not yet recorded using data from Third Party Payment Systems and estimates of costs incurred when goods or services received but not invoiced.

**Advances from Others and Deferred Revenue:** Advances from Others and Deferred Revenue are cash received in advance of goods or services that have not been fully rendered.

## N. Environmental and Disposal Liabilities

E&DL are a probable and reasonably estimable future outflow or expenditure of resources that exists as of the financial reporting date for environmental cleanup costs resulting from past transactions or events.

The DLA NDSTF is responsible for accurate reporting of E&DL and expenses for the real property and/or equipment that it records and reports in its financial statements as assets, regardless of ownership by any Federal agency. DLA NDSTF identifies, and estimates accrued E&DL through its annual CTC process. DLA NDSTF's accrued E&DL comprises of environmental cleanup costs associated with restoration of environmental sites on real property that it does not own, but has received budget authority to execute and manage. These environmental sites may include, but are not limited to, decontamination, decommissioning, site restoration, site monitoring, clean closure of assets, and post- closure costs related to the Agency's operations that result in hazardous waste.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities and Commitments and Contingencies; Note 7, *Environmental and Disposal Liabilities,* and Note 9, *Commitments and Contingencies*.)

## O. Payroll and Annual Leave Accruals

Accrued payroll consists of salaries, wages, and other compensation earned by employees, but not yet disbursed as of the Balance Sheet dates. DLA NDSTF accrues the cost of unused annual leave, including restored leave, compensatory time, and credit hours as earned and reduces the accrual when leave is taken. The payroll and annual leave accrual liability is accrued based on the latest pay period data for reporting purposes (refer to Note 8, *Other Liabilities*).

## P. Federal Employee Benefits Payable

The FECA (Public Law 103-3) provides income and medical cost protection to covered Federal civilian employees injured on the job, to employees who have incurred work-related occupational diseases, and to beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. The FECA program is administered by DOL, which pays valid claims and subsequently seeks reimbursement from DLA NDSTF for these paid claims. The FECA liability consists of two elements.

The first element, accrued FECA liability, is based on actual future payments for claims paid by DOL but not yet reimbursed by DLA NDSTF. DLA NDSTF reimburses DOL for claims as funds are appropriated for this purpose. In general, there is a one to two- year period between payment by DOL and reimbursement to DOL by DLA NDSTF. As a result, DLA NDSTF recognizes an intragovernmental liability, not covered by budgetary resources, for the claims paid by DOL that will be reimbursed by DLA NDSTF.

The second element, actuarial FECA liability, is the estimated liability for future payments and is recorded as an Other than Intragovernmental liability, not covered by budgetary resources. The actuarial FECA liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. DOL determines the actuarial FECA liability annually, as of September 30, using an actuarial method that considers historical benefit payment patterns, wage inflation factors, medical inflation factors, and other variables. The projected annual benefit payments are discounted to present value. The methodology for billable projected liabilities includes, among other things: (1) an algorithmic model that relies on individual case characteristics and benefit payments (the FECA Case Reserve Model) and (2) incurred but not reported claims were estimated using historical incurred benefit liabilities and payments.

(Refer to Note 5, *Liabilities Not Covered by Budgetary Resources* and Note 6, *Federal Employee Benefits Payable and Related Other Liabilities*.)

## Q. Pension Benefits

Based on the effective Federal government start date, DLA NDSTF's civilian employees participate in either the CSRS, a defined benefit plan, or the FERS, a defined benefit plan and contribution plan. The employee pension benefit is managed at the OUSD level. The measurement of the service cost requires the use of an actuarial cost method and assumptions. The OPM administers these benefits and provides the factors that DLA NDSTF applies to calculate and recognize imputed costs, as reported in its Statements of Net Cost, and a corresponding imputed revenue in the Statements of Changes in Net Position. DLA NDSTF is not responsible for and does not report CSRS or FERS assets, accumulated plan benefits, or liabilities applicable to its employees. OPM is responsible for and reports these amounts.

## R. Net Position

Net position is the residual difference between assets and liabilities and consists of unexpended appropriations and cumulative results of operations.

**Unexpended Appropriations:** Unexpended appropriations consist of unobligated and undelivered order balances. Unobligated balances are amounts of remaining budgetary resources available for obligation, which have not been rescinded or withdrawn. Undelivered orders are the amount of obligations incurred for goods and/or services ordered, but not yet received.

**Cumulative Results of Operations:** Cumulative results of operations consist of the net difference since inception between: (1) expenses and losses; (2) revenue and gains; and (3) other financing sources.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Revenue, and Gains, Inventory and Related Property, Net, and Accounts Payable, Expenses, and Undelivered Orders).

## S. Revenue and Other Financing Sources

**Exchange and Non-exchange Revenue:** The DLA NDSTF classifies revenue as either exchange revenue or non-exchange revenue. Exchange revenue arises when DLA NDSTF sells the materials that have been deemed excess to the needs of the stockpile. The proceeds from the sale of materials are DLA NDSTF's major financing source and are used to fund the operation. In addition, materials are offered for sale on the open market and are awarded through competitive bidding.

Non-exchange revenue is derived from the government's sovereign right to demand payment, such as specifically identifiable, legally enforceable claims. Non-exchange revenue is considered to impact the cost of operations and is reported in the Statements of Changes in Net Position as a financing source. For the years ended September 30, 2023 and 2022, respectively, DLA NDSTF does not have activity related to non-exchange revenue.

**Other Financing Sources:** Other financing sources, other than exchange and non-exchange revenue, include additional inflows of resources that increase results of operations during the reporting period. DLA NDSTF's other financing sources come from appropriations received and recognized as financing sources when used.

**Imputed Financing and Imputed Cost:** In certain cases, DLA NDSTF receives goods and services from other Federal entities at no cost or at a cost less than the full cost to the providing entity. Consistent with accounting standards, certain costs of the providing entity that are not fully reimbursed by DLA NDSTF are recognized as imputed cost in the Statements of Net Cost and are offset by imputed financing in the Statements of Changes in Net Position. DLA NDSTF recognizes the following imputed cost and related imputed financing: (1) employee benefits administered by the OPM (i.e., retirement, health, life insurance benefits); and (2) claims settled by the Treasury Judgment Fund in accordance with SFFAS 55, *Amending Inter- Entity Costs Provisions*.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Inter-Entity Cost, Accounts Receivable, Revenue, and Gains and Inventory and Related Property, Net.)

### T. Expenses

Expenses are recognized when there are outflows, usage of assets, or incurrences of liabilities (or a combination) from carrying out activities related to DLA NDSTF's program and missions, for which benefits do not extend beyond the present operating period. For financial reporting purposes, operating expenses are recognized in the period incurred.

(refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payable, Expenses, and Undelivered Orders).

# Note 2: Fund Balance with Treasury (Unaudited)

Fund Balance with Treasury as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Status of Fund Balance with Treasury** | | |
| Unobligated Balance: | | |
| Available | $ 196,826 | $ 166,499 |
| Unavailable | 290,050 | 291,545 |
| Obligated Balances Not Yet Disbursed | 92,926 | 42,583 |
| **Total Fund Balance with Treasury** | **$ 579,802** | **$ 500,627** |

**Status of Fund Balance with Treasury** presents the budgetary and proprietary resources that constitute DLA NDSTF FBwT. It consists of unobligated and obligated balances. Unobligated and obligated balances differ from the related amounts reported in the Statements of Budgetary Resources because budgetary balances are supported by amounts other than FBwT.

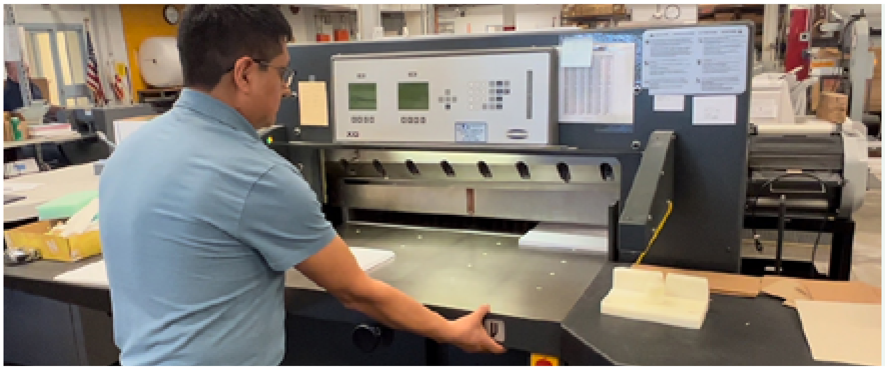
**Unobligated Balance - Available** includes the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations and can be used for future obligations.

**Unobligated Balance - Unavailable** includes the cumulative amount of unapportioned funds not available for obligation from offsetting collections.

**Obligated Balances Not Yet Disbursed** includes funds that have been obligated for goods and services not received and those received but not paid.

**Non-budgetary FBwT** consists of FBwT in unavailable receipt accounts and clearing accounts that do not have budgetary authority and non-budgetary FBwT such as non-fiduciary deposit funds. As of September 30, 2023 and 2022, DLA TF does not have a balance for non-budgetary FBwT.

**Other Information** includes the following tables summarizing the undistributed collections and disbursements between U.S. Treasury and DLA NDSTF as of September 30, 2023 and 2022, respectively.



**Document Services in Quantico**

Defense Logistics Agency Document Services member Herbert Curisinche, a document automation specialist, operates a paper cutter at the Quantico, Virginia field site.

**Photo By:** Jason Shamberger

| FY 2023 Adjustments of Undistributed Collections and Disbursements (dollars in thousands) | | | |
|---|---|---|---|
| **Transaction Type** | **Treasury Balance based on CARS** | **DLA TF Trial Balance** | **Balances Not Yet Recorded in DLA Accounting System - Undistributed** |
| Collections | $ 45,009 | $ 45,009 | $ - |
| Disbursements | $ 79,334 | $ (79,424) | $ (89) |

| FY 2022 Adjustments of Undistributed Collections and Disbursements (dollars in thousands) | | | |
|---|---|---|---|
| **Transaction Type** | **Treasury Balance based on CARS** | **DLA TF Trial Balance** | **Balances Not Yet Recorded in DLA Accounting System - Undistributed** |
| Collections | $ 102,262 | $ 102,262 | $ - |
| Disbursements | $ 40,268 | $ 39,675 | $ 593 |

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Fund Balance with Treasury)

# Note 3: Inventory and Related Property, Net (Unaudited)

Inventory and Related Property, Net as of September 30, 2023 and 2022, respectively, include stockpile materials and consist of the following (dollars in thousands):

| | Valuation Method | FY 2023 | FY 2022 |
|---|---|---|---|
| **Inventory and Related Property, Net** | | | |
| Stockpile Materials Held for Sale | HC | $ 15,067 | $ 11,877 |
| Stockpile Materials Held in Reserve for Future Use | HC | 369,575 | 750,704 |
| **Total Inventory and Related Property, Net** | | **$ 384,642** | **$ 762,581** |

HC = Historical Cost[19]

**Stockpile Materials Held for Sale** is comprised of materials deemed to be excess and have been identified for disposal based on the Annual Sales Plan (ASP). The Stockpile Materials Held for Sale in FY 2023 includes Ores, Metals, and Minerals. As of September 30, 2023 and 2022, Stockpile Materials Held for Sale estimated selling price is $15.1 million and $39.1 million, respectively. The difference between the carrying amount of the Stockpile Materials Held for Sale and the estimated selling price as of September 30, 2023 and 2022, is $0.02 million and $(27.3) million, respectively.

**Stockpile Materials Held in Reserve for Future Use** consist of a variety of industrial commodities including base and minor metals, ferrous and non-ferrous ores, metal powders and mercury.

Based on the Mercury Export Ban Act that was signed into law on October 14, 2008, Federal agencies are prohibited from conveying, selling, or distributing metallic mercury that is under their control or jurisdiction. This includes stockpiles held by DoD. Beginning January 1, 2013, United States Federal agencies are prohibited from the export of metallic mercury.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Receivable, Revenue; Accounts Payable, Expenses, and Undelivered Orders; and Gains, and Inventory and Related Property, Net.)

[19]The DoD cost flow assumption policy for Inventory and Related Property is Moving Average Cost (MAC); DLA SM, due to the nature of its operations, does not rely upon its cost flow assumption to determine Historical Cost as all inventory is specifically identifiable.

# Note 4: General Property, Plant and Equipment, Net (Unaudited)

General Property, Plant and Equipment, Net as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | | | |
|---|---|---|---|
| | Acquisition Value | Accumulated Depreciation | Net Book Value |
| **Major Asset Class:** | | | |
| General Equipment | $ 2,223 | $ (1,871) | $ 352 |
| **Total General Property, Plant and Equipment, Net** | **$ 2,223** | **$ (1,871)** | **$ 352** |

| FY 2022 | | | |
|---|---|---|---|
| | Acquisition Value | Accumulated Depreciation | Net Book Value |
| **Major Asset Class:** | | | |
| General Equipment | $ 2,223 | $ (1,649) | $ 574 |
| **Total General Property, Plant and Equipment, Net** | **$ 2,223** | **$ (1,649)** | **$ 574** |

The table below discloses activity for General Property, Plant and Equipment, Net as of September 30, 2023 and 2022, respectively (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **General Property, Plant and Equipment, Net - Beginning Balances** | **$ 574** | **$ 797** |
| Depreciation Expense | (222) | (223) |
| **General Property, Plant and Equipment, Net - Ending Balances** | **$ 352** | **$ 574** |

### Ukraine Support

Soldiers assigned to the 841st Transportation Battalion park Bradley fighting vehicles within the ARC Integrity vehicle carrier in North Charleston, S.C., Jan. 25, 2023. More than 60 Bradleys were shipped by U.S. Transportation Command as part of the U.S. military aid package to Ukraine. **Photo By:** Oz Suguitan, U.S. Transportation Command

# Note 5: Liabilities not Covered by Budgetary Resources (Unaudited)

Liabilities not Covered by Budgetary Resources as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Intragovernmental Liabilities** | | |
| Other Liabilities | $ 178 | $ 178 |
| **Total Intragovernmental Liabilities** | **178** | **178** |
| **Other than Intragovernmental Liabilities** | | |
| Environmental and Disposal Liabilities | 10,056 | 11,600 |
| Federal Employee Benefits Payable | 2,383 | 2,050 |
| **Total Other than Intragovernmental Liabilities** | **12,439** | **13,650** |
| **Total Liabilities Not Covered by Budgetary Resources** | **12,617** | **13,828** |
| **Total Liabilities Covered by Budgetary Resources** | **2,893** | **3,152** |
| **Total Liabilities not Requiring Budgetary Resources** | **5** | **-** |
| **Total Liabilities** | **$ 15,515** | **$ 16,980** |

**Other Liabilities (Intragovernmental)** include the accrued FECA liability paid by DOL but not yet reimbursed by DLA NDSTF.

**Environmental and Disposal Liabilities (Other than Intragovernmental)** consist of probable and reasonably estimable future outflow or expenditure of resources that exist as of the financial reporting date for environmental cleanup costs resulting from past transactions or events. As of September 30, 2023 and 2022, the total liabilities covered by budgetary resources for environmental and disposal liabilities consist of $1.7 million and $581.7 thousand, respectively.

**Federal Employee Benefits Payable (Other than Intragovernmental)** are comprised of the current year FECA actuarial liability based on DOL records, and current year unfunded annual leave earned by civilian employees but not yet paid. Unfunded annual leave includes restored leave, compensatory time, and credit hours as earned.

**Liabilities Not Requiring Budgetary Resources** consist of Liabilities for Nonfiduciary Deposit Funds and Undeposited Collections that will not require the use of Budgetary resources.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Accounts Payables, Expenses, and Undelivered Orders and Accounts Receivable, Revenue, and Gains; Note 6, *Federal Employee Benefits Payable and Related Other Liabilities*; and Note 7, *Environmental and Disposal Liabilities.*)

**Royal Navy's Next Chief of Defense Logistics and Support**

British Royal Navy Adm. Andy Kyte, third from left, met with Defense Logistics Agency Aviation Commander Air Force Brig. Gen. Sean Tyler and other senior DLA Aviation leaders during his visit to Defense Supply Center Richmond, Virginia, March 23, 2023. **Photo By:** Navy Lt. Gregory Shumaker, Aide-de-Camp

# Note 6: Federal Employee Benefits Payable and Related Other Liabilities (Unaudited)

Federal Employee Benefits Payable and Related Other Liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | Liabilities | (Less: Assets Available to Pay Benefits) | Unfunded Liabilities |
|---|---|---|---|
| **Intragovernmental Other Liabilities** | | | |
| Employer Contributions and Payroll Taxes Payable | $ 55 | $ (55) | $ - |
| Unfunded FECA Liability | 178 | - | 178 |
| **Total Intragovernmental Other Liabilities** | **$ 233** | **$ (55)** | **$ 178** |
| **Other than Intragovernmental Federal Employee Benefits Payable** | | | |
| Actuarial FECA Liability | $ 1,704 | $ - | $ 1,704 |
| Accrued Unfunded Annual Leave | 751 | (72) | 679 |
| **Total Other than Intragovernmental Federal Employee Benefits Payable** | **$ 2,455** | **$ (72)** | **$ 2,383** |

| FY 2022 | Liabilities | (Less: Assets Available to Pay Benefits) | Unfunded Liabilities |
|---|---|---|---|
| **Intragovernmental Other Liabilities** | | | |
| Employer Contributions and Payroll Taxes Payable | $ 56 | $ (56) | $ - |
| Unfunded FECA Liability | 178 | - | 178 |
| **Total Intragovernmental Other Liabilities** | **$ 234** | **$ (56)** | **$ 178** |
| **Other than Intragovernmental Federal Employee Benefits Payable** | | | |
| Actuarial FECA Liability | $ 1,320 | $ - | $ 1,320 |
| Accrued Unfunded Annual Leave | 730 | - | 730 |
| **Total Other than Intragovernmental Federal Employee Benefits Payable** | **$ 2,050** | **$ -** | **$ 2,050** |

**Employer Contributions and Payroll Taxes Payable (Intragovernmental)** are the employer portion of payroll taxes and benefit contributions for health benefits, retirement, life insurance and voluntary separation incentive payments.

**Unfunded FECA Liability (Intragovernmental)** includes the accrued FECA liability paid by DOL but not yet reimbursed by DLA NDSTF.

**Actuarial FECA Liability (Other than Intragovernmental)** are workers' compensation benefits developed by the DOL's OWCP and provided to DLA NDSTF at the end of each FY. 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 OMB's economic assumptions for 10-year U.S. Treasury notes and bonds. COLAs and medical inflation factors are also applied to the calculation of projected future benefits.

**Accrued Unfunded Annual Leave (Other than Intragovernmental)** includes restored leave, compensatory time, and credit hours as earned.

(Refer to Note 5, *Liabilities Not Covered by Budgetary Resources*.)

# Note 7: Environmental and Disposal Liabilities (Unaudited)

Environmental and Disposal Liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Environmental and Disposal Liabilities** | | |
| Environmental Corrective Action | $ 11,707 | $ 12,090 |
| Environmental Closure Requirements | - | 91 |
| **Total Environmental and Disposal Liabilities** | **$ 11,707** | **$ 12,181** |

**The DLA NDSTF E&DL are comprised of two primary elements:** (1) existing obligations supporting DLA NDSTF environmental restoration programs, and (2) the CTC which includes anticipated future costs necessary to complete environmental restoration requirements at DLA SM environmental restoration sites.

In FY 2023 and FY 2022, DLA NDSTF utilized the RACER software to generate the CTC estimates of anticipated future costs. As of September 30, 2023 and 2022, the total NDSTF E&DL consist of $11.7 million and $12.2 million, respectively.

FY 2023 cost estimates under DLA Strategic Materials were generated for sites with environmental corrective action costs.

Per DoD policy and FASAB guidance, Military Departments are responsible for reporting the entirety of E&DL associated with real property located on their installations for Environmental Closure Requirements E&DL. Accordingly, as of September 30, 2023, DLA NDSTF has no reportable Environmental Closure Requirements E&DL.

**Types of Environmental and Disposal Liabilities:** The DLA NDSTF is responsible for the recognition, measurement, reporting, and disclosure of Non-BRAC E&DL and Environmental Disposal for General Equipment. Non-BRAC E&DL are specifically related to past and current installation restoration activities and operations. All cleanup and disposal actions are done in coordination with regulatory agencies, other responsible parties, and current property owners.

The DLA NDSTF reportable E&DL is under Other Accrued E&DL – Non- BRAC and includes the following line items:

Environmental Corrective Action includes E&DL associated with the cleanup sites not eligible for DERP funding, typically conducted under the RCRA or other Federal or state statutes and regulations.

The DLA assessed its real property and General Equipment inventories and does not currently have reportable NDSTF E&DL for Environmental Closure, Asbestos, and General Equipment.

Beginning in FY 2023, DLA fully reduced its recognized NDSTF Environmental Closure Requirements E&DL balances to zero, in accordance with the September 2022 OUSD(C) memorandum clarifying that installation hosts are responsible for recognizing E&DL related to real property assets regardless of which entity funds and executes the closure activities.

There are no other E&DL categories as listed on the DoD 7000.14-R Financial Management Regulation (FMR) Volume 6B, Chapter 10 – *Note to the Financial Statements*, Paragraph 1017, Figure 10-31. *Environmental and Disposal Liabilities* (February 2023).

**Applicable Laws and Regulations for Cleanup Requirements:** The DLA NDSTF 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. DLA NDSTF is required to comply with the following laws and regulations for corrective action where applicable: The Comprehensive Environmental Response, Compensation, and Liability Act; the Superfund Amendments and Reauthorization Act; RCRA; and other applicable Federal, State, and local laws and regulations. Required cleanup may at times extend beyond DLA SM operational site boundaries onto adjacent property or onto other sites where DLA SM is named as a potentially responsible party by a regulatory agency. DLA NDSTF reports corrective action related E&DL in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government,* and Federal Financial Accounting Technical Release 2, *Determining Probable* and *Reasonably Estimable for Environmental Liabilities in the Federal Government.*

The DLA NDSTF is no longer required to report asset related E&DL for assets it is not reporting on its financial statements due to policy changes to the DoD 7000.14-R FMR Volume 4 Chapter 13 – *Environmental and Disposal Liabilities* (March 2022), FASAB Interpretation of Federal Financial Accounting Standards 9, *Cleanup Cost Liabilities Involving Multiple Component Reporting Entities: An Interpretation of SFFAS 5 & SFFAS 6*, and the resulting September 2022 OUSD(C) memorandum clarifying that installation hosts are responsible for recognizing E&DL related to real property assets regardless of which entity funds and executes the closure activities.

**Methods for Assigning Estimated Total Cleanup Cost to Current Operating Periods:** To estimate future environmental costs, DLA NDSTF utilizes a combination of historical or pre-negotiated contract costs, proposal costs, engineering estimates, and in the absence of other detailed information, parametric estimates created using the RACER software. Any historical costs used in the creation of the estimates for DLA NDSTF E&DL are adjusted for inflation and reported in current year dollars. The RACER Steering Committee ensures that the RACER software is VV&A in accordance with DoD Instruction 5000.61 - *DoD Modeling and Simulation (M&S) Verification, Validation, and Accreditation*. The DoD is working with the RACER Steering Committee and stakeholders to identify improvements to RACER functionality, auditability, and documentation. Detailed information on the estimating methodologies are provided in the DLA ELM SOPs.

**Nature of Estimates and the Disclosure of Information Regarding Possible Changes Due to Inflation, Deflation, Technology, or Applicable Laws and Regulations:** The DLA NDSTF E&DL Site ID process tracks environmental events such as spills and releases in an Environmental Event Repository and evaluates each event annually for E&DL potentiality to determine the annual CTC inventory. DLA NDSTF CTC estimates are created annually for all projected requirements and are finalized and approved by July. The estimates are then reevaluated through a roll forward review to identify any material changes to previously approved estimates as of September 30. Processes are conducted in accordance with DLA policies and procedures, the DoD 7000.14-R FMR Volume 4, Chapter 13 – *Environmental and Disposal Liabilities* (March 2022).

CTC estimates revised through roll forward, as applicable, and prior year obligations are reported in the balance as of September 30. As of the reporting date, no material changes in the total estimated cleanup costs were identified through the roll forward review due to changes in laws, technology, or plans.

Beginning in FY 2023, DLA fully reduced its NDSTF recognized Environmental Closure Requirements E&DL balance to zero, in accordance with the September 2022 OUSD(C) memorandum clarifying that installation hosts are responsible for recognizing E&DL related to real property assets regardless of which entity funds and executes the closure activities. In addition, DLA is not aware of any other changes to NDSTF E&DL estimates that would result from inflation, deflation, technology, plans, and or pending changes to applicable laws and regulation. The cost estimate changes from prior periods are primarily driven by remediation activities and operations, as evidenced by UDOs; there are minor adjustments for inflation or other similar administrative costs throughout the fiscal year. E&DL estimates will be reevaluated each year and may change in the future due to changes in laws and regulations, changes in agreements with regulatory agencies, and advances in technology.

**Uncertainty Regarding the Accounting Estimates Used to Calculate the Reported Environmental and Disposal Liabilities:** The stated total NDSTF E&DL includes prior year obligations and the estimates of future costs necessary to complete requirements. DLA NDSTF has instituted extensive controls to ensure that these estimates are accurate and reproducible. The cost estimates produced through the ELM process are considered accounting estimates, which require certain judgments and assumptions that are reasonable based upon information available at the time the estimates are calculated. Actual results may materially vary from the accounting estimates if agreements with regulatory agencies require remediation or closure activities to a different degree than anticipated when calculating the estimates. NDSTF E&DL can be further affected if investigation of the environmental sites reveals contamination levels that differ from the estimate parameters.

The DLA NDSTF utilizes a formalized Site ID process to identify, track, and evaluate environmental events where the potential for an out-year E&DL exists but the E&DL is not probable and measurable. These environmental events will be re-evaluated in the following fiscal year to determine if any changes have taken place and sufficient information/data is available to create an estimate of future costs that would be included in the NDSTF E&DL balance.

**Unrecognized Costs:** The DLA NDSTF has no unrecognized cost as there are no reportable Asset-related Environmental Closure Requirements, Asbestos, and General Equipment related E&DL.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to *Environmental and Disposal Liabilities and Commitments and Contingencies.)*

# Note 8: Other Liabilities (Unaudited)

Other Liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | Current | Noncurrent | Total |
|---|---|---|---|
| **Other than Intragovernmental Other Liabilities** | | | |
| Accrued Funded Payroll and Benefits | $ 280 | $ - | $ 280 |
| Deposit Funds and Suspense Accounts | 5 | - | 5 |
| **Total Other than Intragovernmental Other Liabilities** | **$ 285** | **$ -** | **$ 285** |

| FY 2022 | Current | Noncurrent | Total |
|---|---|---|---|
| **Other than Intragovernmental Other Liabilities** | | | |
| Accrued Funded Payroll and Benefits | $ 366 | $ - | $ 366 |
| Deposit Funds and Suspense Accounts | - | - | - |
| **Total Other than Intragovernmental Other Liabilities** | **$ 366** | **$ -** | **$ 366** |

**Accrued Funded Payroll and Benefits (Other than Intragovernmental)** include salaries, wages, and other compensation earned by employees but not yet disbursed.

**Deposit Funds and Suspense Accounts (Other than Intragovernmental)** include collections for which DLA TF has not yet received a deposit confirmation from Treasury.

# Note 9: Commitments and Contingencies (Unaudited)

Accrued and reasonably possible environmental contingent liabilities as of September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| FY 2023 | Accrued Liabilities | Estimated Range of Loss | |
|---|---|---|---|
| | | Lower End | Upper End |
| **Environmental Contingencies** | | | |
| Probable | $ 11,707 | $ - | $ - |
| Reasonably Possible | $ - | $ - | $ - |

| FY 2022 | Accrued Liabilities | Estimated Range of Loss | |
|---|---|---|---|
| | | Lower End | Upper End |
| **Environmental Contingencies** | | | |
| Probable | $ 12,181 | $ - | $ - |
| Reasonably Possible | $ - | $ - | $ - |

**Environmental Contingencies:** The DLA NDSTF has developed a process to identify, estimate, and record contingent E&DL. DLA NDSTF does not estimate a potential range of loss in this process. Where DLA NDSTF is aware of probable and measurable future outflow of resources due to a past event or exchange transaction, the appropriate program categories are reported in Note 7, *Environmental and Disposal Liabilities*.

**Legal Contingencies:** The DLA NDSTF was not a party in administrative proceedings or legal actions as of September 30, 2023 and 2022. DLA's EWSC is used by the Office of General Counsel to report the outcomes and possible liability amounts of open cases.

Cases for which legal counsel determines an adverse outcome is reasonably possible and the possible financial outflow is measurable, are not recorded, but disclosed as reasonably possible for financial reporting purposes.

As of September 30, 2023, DLA has zero matters that are identified as a probable or reasonably possible liability, and zero matters that are identified as remote liabilities.

**Commitments:** The DLA NDSTF does not have obligations related to canceled appropriations for contractual commitments.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Environmental and Disposal Liabilities and Commitments and Contingencies; Note 5, *Liabilities Not Covered by Budgetary Resources*; and Note 7, *Environmental and Disposal Liabilities*.)

# Note 10: Statement of Budgetary Resources (Unaudited)

**Unobligated Balance Brought Forward, October 1:** There were no adjustments during the current year to correct the unobligated balance brought forward, October 1. Components of the amount reported as "Unobligated Balance from Prior Year Budget Authority, net" are disclosed in the table below. Other adjustments consist of recoveries of prior year obligated balances. The following table displays a reconciliation between the prior year's unobligated balance, end of year amount to the current year's unobligated balance from prior year budget authority, net amount (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Reconciliation of PY Ending Unobligated Balances of CY Beginning Unobligated Balances** | | |
| Unobligated balance brought forward, October 1 | $ 428,341 | $ 261,719 |
| Recoveries of prior year unpaid obligations | 1,843 | 1,689 |
| **Unobligated balance, total** | **$ 430,184** | **$ 263,408** |

**Undelivered Orders (UDOs):** For the years ended September 30, 2023 and 2022, respectively, consist of the following (dollars in thousands):

| | FY 2023 | FY 2022 |
|---|---|---|
| **Intragovernmental Undelivered Orders** | | |
| Unpaid | $ 64,365 | $ 21,324 |
| Paid | 24,315 | - |
| **Total Intragovernmental Undelivered Orders** | **88,680** | **21,324** |
| **Other than Intragovernmental Undelivered Orders** | | |
| Unpaid | 27,318 | 19,334 |
| Paid | 1,238 | 1,460 |
| **Total Other than Intragovernmental Undelivered Orders** | **28,556** | **20,794** |
| **Total Undelivered Orders** | **$ 117,236** | **$ 42,118** |

UDOs represent the amount of goods and/or services ordered to perform DLA NDSTF's mission objectives that have not been received. Unpaid UDOs represent obligations for goods and services that have not been received or paid. Whereas paid UDOs represent obligations for goods and services that have been paid for in advance of receipt.

Due to system limitations, DLA NDSTF is unable to determine the Intragovernmental and Other than Intragovernmental allocation of unpaid UDOs. DLA NDSTF estimates the allocation of Intragovernmental and Other than Intragovernmental unpaid UDOs based on funded liabilities and excluding payroll and employee benefit liabilities.

(Refer to Note 1.C., *Departures from U.S. GAAP*, related to Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions and Accounts Payable, Expenses, Undelivered Orders.)

# Note 11: Reconciliation of Net Cost to Net Outlays (Unaudited)

Reconciliation of Net Cost to Net Outlays for the years ended September 30, 2023 and 2022, consist of the following (dollars in thousands):

| FY 2023 | Intragovernmental | Other than Intragovernmental | Total |
|---|---|---|---|
| **NET COST** | **$ 10,659** | **$ 376,976** | **$ 387,635** |
| **Components of Net Cost That are Not Part of Net Outlays** | | | |
| General Property Plant and Equipment Depreciation | - | (222) | (222) |
| Cost of Goods Sold | - | (18,856) | (18,856) |
| Net Gains/(Losses) | - | 596 | 596 |
| Net Gains/(Losses) Related to Inventory Valuation Adjustment | - | (378,819) | (378,819) |
| **Increase/(Decrease) in Assets:** | | | |
| Cash and Other Monetary Assets | - | 5 | 5 |
| Accounts Receivable, Net | - | (24) | (24) |
| Advances and Prepayments | 24,315 | (222) | 24,093 |
| **(Increase)/Decrease in Liabilities:** | | | |
| Accounts Payable | 204 | 466 | 670 |
| Environmental and Disposal Liabilities | - | 474 | 474 |
| Federal Employee Benefits Payable | - | (405) | (405) |
| Advances from Others and Deferred Revenue | - | 644 | 644 |
| Other Liabilities | 1 | 81 | 82 |
| **Financing Sources:** | | | |
| Imputed Financing | (688) | - | (688) |
| **Total Components of Net Cost That are Not Part of Net Outlays** | **23,832** | **(396,282)** | **(372,450)** |
| **Components of Net Outlays That are Not Part of Net Cost** | | | |
| Acquisition of Inventory | - | 19,140 | 19,140 |
| **Total Components of Net Outlays That are Not Part of Net Cost** | **-** | **19,140** | **19,140** |
| **NET OUTLAYS** | **$ 34,491** | **$ (166)** | **34,325** |
| **Outlays, Net, Statement of Budgetary Resources** | | | **34,325** |
| **Reconciling Difference** | | | **$ -** |

| FY 2022 | | | |
|---|---|---|---|
| | Intragovernmental | Other than Intragovernmental | Total |
| **NET COST** | **$ 16,977** | **$ (28,708)** | **$ (11,731)** |
| **Components of Net Cost That are Not Part of Net Outlays** | | | |
| General Property Plant and Equipment Depreciation | - | (223) | (223) |
| Cost of Goods Sold | - | (50,276) | (50,276) |
| Net Gains/(Losses) | - | (15) | (15) |
| Net Gains/(Losses) Related to Inventory Valuation Adjustment | - | - | - |
| **Increase/(Decrease) in Assets:** | | | |
| Cash and Other Monetary Assets | - | - | - |
| Accounts Receivable, Net | - | 30 | 30 |
| Advances and Prepayments | - | 545 | 545 |
| **(Increase)/Decrease in Liabilities:** | | | |
| Accounts Payable | (28) | (394) | (422) |
| Environmental and Disposal Liabilities | - | (2,381) | (2,381) |
| Federal Employee Benefits Payable | - | 122 | 122 |
| Advances from Others and Deferred Revenue | - | (644) | (644) |
| Other Liabilities | 48 | (104) | (56) |
| **Financing Sources:** | | | |
| Imputed Financing | (503) | - | (503) |
| **Total Components of Net Cost That are Not Part of Net Outlays** | **(483)** | **(53,340)** | **(53,823)** |
| **Components of Net Outlays That are Not Part of Net Cost** | | | |
| Acquisition of Inventory | - | 3,560 | 3,560 |
| **Total Components of Net Outlays That are Not Part of Net Cost** | **-** | **3,560** | **3,560** |
| **NET OUTLAYS** | **$ 16,494** | **$ (78,488)** | **(61,994)** |
| **Outlays, Net, Statement of Budgetary Resources** | | | **(61,994)** |
| **Reconciling Difference** | | | **$ -** |

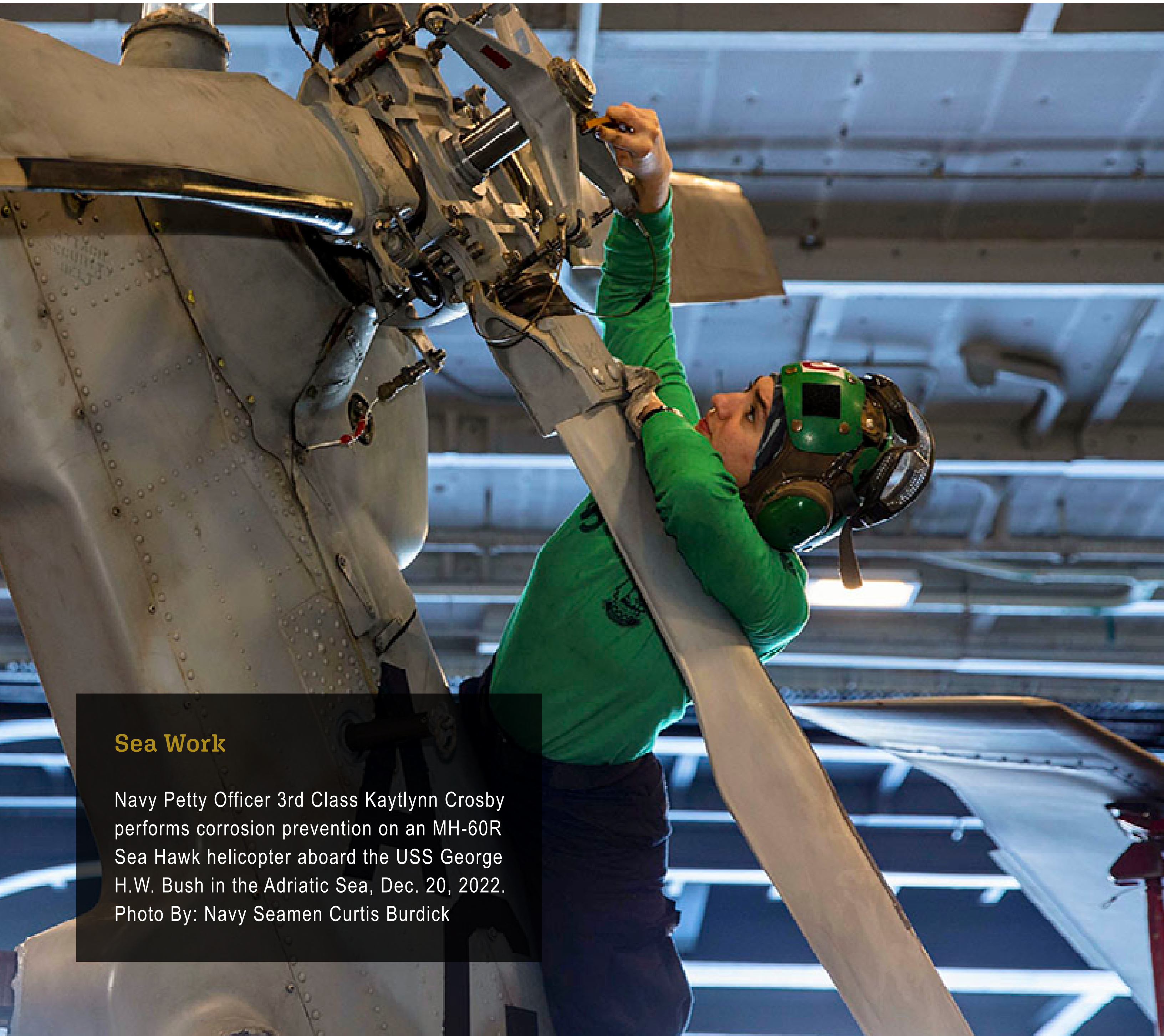
The Net Cost to Net Outlays Reconciliation schedule reconciles the Net Cost (reported in the Statements of Net Cost) to the Net Outlays (reported in the Statements of Budgetary Resources). The reconciliation clarifies the relationship between budgetary and proprietary accounting information. Examples of the reconciling items identified are: (1) Transactions which did not result in an outlay but did result in a cost; and (2) Unpaid expenses included in the net cost in this reporting period but not yet included in outlays. Components of net cost that are not part of net outlays are most commonly (a) the result of allocating assets to expenses over more than one reporting period (e.g., depreciation); (b) the temporary timing differences between outlays/receipts and the operating expense/revenue during the period; and (c) costs financed by other entities (imputed inter-entity costs).

For FY 2023, the key reconciling differences between the net cost and net outlays for DLA NDSTF include: (1) the Cost of Goods Sold, which related to stockpile material transactions, representing the sales activity for Other than Intragovernmental customers; (2) increase in net losses due stockpile materials valuation adjustments; (3) advances for stockpile material acquisitions not yet received; and (4) the acquisition of inventory.

For FY 2022, the key reconciling differences between the net cost and net outlays for DLA NDSTF include: (1) the Cost of Goods Sold, which related to stockpile material transactions, representing the sales activity for Other than Intragovernmental customers; (2) the increase in Non-BRAC Environmental Corrective Action E&DL; and (3) the acquisition of inventory.

The DLA NDSTF does not have an established policy to identify and reconcile net cost to net outlays and/or identify components of net cost or net outlays that have not been properly accounted for. However, DLA NDSTF will continue to investigate and resolve the causes of the items not included in the reconciliation and any reconciling differences.

(Refer to Note 1.C., Departures from U.S. GAAP, related to Accounts Receivable, Revenue, and Gains, Inventory and Related Property, Net, Intragovernmental/Intra-departmental and Other than Intragovernmental Transactions, Accounts Payable, Undelivered Orders, and Reconciliation of Net Cost to Net Outlays.)



**Sea Work**

Navy Petty Officer 3rd Class Kaytlynn Crosby performs corrosion prevention on an MH-60R Sea Hawk helicopter aboard the USS George H.W. Bush in the Adriatic Sea, Dec. 20, 2022. Photo By: Navy Seamen Curtis Burdick

# Section 3

## *Other Information*

(Unaudited)

◀ **Dragoon Drama**

Soldiers assigned to the 2nd Cavalry Regiment advance on a simulated town during Dragoon Ready 23 at the Joint Multinational Readiness Center in Hohenfels, Germany, Jan. 29, 2023. The exercise included U.S. soldiers and service members from Italy and the United Kingdom.

**Photo By:** Army Spc. Donovon Lynch

# Section 3

## *Other Information* (Unaudited)

### In this section:

# Summary of Financial Statement Audit and Management Assurances

The audit reports on the FY 2023 and FY 2022 DLA WCF, GF, and NDSTF financial statements identified material weaknesses for DLA WCF, GF, and NDSTF. Table 1 below provides a summary of the DLA WCF, GF, and NDSTF financial statement audit results for FY 2023 and FY 2022, as restated (GF only).

Although the material weaknesses overall are not resolved, DLA is continuing to develop CAPs to resolve specific findings associated with the material weaknesses.

**Table 1: DLA WCF Summary of the Financial Statement Audit**

| Audit Opinion | Disclaimer | | | | |
|---|---|---|---|---|---|
| Restatement | No | | | | |
| Material Weaknesses | Beginning Balance | New | Resolved | Consolidated | Ending Balance |
| Inventory | 1 | - | - | - | 1 |
| Fund Balance with Treasury | 1 | - | - | - | 1 |
| Accounts Receivable and Revenue | 1 | - | - | - | 1 |
| Accounts Payable and Expenses | 1 | - | - | - | 1 |
| Financial Reporting | 1 | - | - | - | 1 |
| Oversight and Monitoring | 1 | - | - | - | 1 |
| Information Systems | 1 | - | - | - | 1 |
| **Total Material Weaknesses** | **7** | **-** | **-** | **-** | **7** |


**Kits for F-35**

A DLA Distribution Hill AFB, Utah, Warehouse Specialist pulls special supplies as she prepares kits for F-35 maintainers. April 12, 2022. Photo taken by Nutan Chada, DLA Public Affairs. **Photo by:** Courtesy of DLA

| FY 2023 DLA GF Summary of the Financial Statement Audit | | | | | |
|---|---|---|---|---|---|
| Audit Opinion | Disclaimer | | | | |
| Restatement | Yes | | | | |
| Material Weaknesses | Beginning Balance | New | Resolved | Consolidated | Ending Balance |
| Property, Plant & Equipment | 1 | - | | - | 1 |
| Fund Balance with Treasury | 1 | - | - | - | 1 |
| Accounts Receivable and Revenue | 1 | - | - | - | 1 |
| Accounts Payable and Expenses | 1 | - | - | - | 1 |
| Financial Reporting | 1 | - | - | - | 1 |
| Oversight and Monitoring | 1 | - | - | - | 1 |
| Information Systems | 1 | - | - | - | 1 |
| Accounting for Long-Term Contracts | - | 1 | - | - | 1 |
| Total Material Weaknesses | 7 | 1 | - | - | 8 |

| FY 2023 DLA NDSTF Summary of the Financial Statement Audit | | | | | |
|---|---|---|---|---|---|
| Audit Opinion | Disclaimer | | | | |
| Restatement | No | | | | |
| Material Weaknesses | Beginning Balance | New | Resolved | Consolidated | Ending Balance |
| Inventory | 1 | - | | - | 1 |
| Fund Balance with Treasury | 1 | - | - | - | 1 |
| Accounts Payable and Expenses | 1 | - | - | - | 1 |
| Financial Reporting | 1 | - | - | - | 1 |
| Oversight and Monitoring | 1 | - | - | - | 1 |
| Information Systems | 1 | - | - | - | 1 |
| Total Material Weaknesses | 6 | - | - | - | 6 |

The DLA SOA package only includes self-identified material weaknesses and significant deficiencies for internal DoD reporting; however, DLA continues to monitor the WCF, GF, and NDSTF financial statement audit material weakness areas separately. DLA's FY 2023 Material Weaknesses and Significant Deficiencies template does not include self-identified material weaknesses in the area of Internal Controls over Operations (ICOR-O). For FY 2023, DLA has completed and validated corrective actions for one ICOR-O Material Weakness, summarized in the table below. In FY 2023, the six WCF Internal Controls over Financial Reporting (ICOFR) material weaknesses, six GF ICOFR material weaknesses, five NDSTF ICOFR material weaknesses, and four DLA Internal Controls over Financial Systems (ICOFS) non-conformances were based on financial statement audit NFRs. However, DLA has determined these audits identified ICOFR material weaknesses and ICOFS non-conformances are still present and have not been remediated in FY 2023. The DLA Audit Coordination & Liaison group continues to separately track WCF, GF, and NDSTF financial statement audit findings and CAPs and report these to the Office of the Deputy Chief Financial Officer.

**Table 2** summarizes DLA's FY 2023 material weaknesses associated with DLA.

| Table 2: Summary of Management Assurances | | | | | | |
|---|---|---|---|---|---|---|
| WCF Effectiveness of Internal Control over Financial Reporting (FMFIA § 2) | | | | | | |
| Statement of Assurance | No Assurance | | | | | |
| Material Weaknesses | Beginning Balance | New | Resolved | Consolidated | Reassessed | Ending Balance |
| Oversight and Monitoring | 1 | - | - | - | - | 1 |
| Financial Reporting | 1 | - | - | - | - | 1 |
| Fund Balance with Treasury | 1 | - | - | - | - | 1 |
| Plan-to-Stock: Inventory | 1 | - | - | - | - | 1 |
| Order-to-Cash: Accounts Receivable and Revenue | 1 | - | - | - | - | 1 |
| Procure-to-Pay: Accounts Payable and Expenses | 1 | - | - | - | - | 1 |
| Total Material Weaknesses | 6 | - | - | - | - | 6 |

| Table 2: Summary of Management Assurances | | | | | | |
|---|---|---|---|---|---|---|
| GF Effectiveness of Internal Control over Financial Reporting (FMFIA § 2) | | | | | | |
| Statement of Assurance | No Assurance | | | | | |
| Material Weaknesses | Beginning Balance | New | Resolved | Consolidated | Reassessed | Ending Balance |
| Acquire-to-Retire: Property, Plant and Equipment | 1 | - | - | - | - | 1 |
| Oversight and Monitoring | 1 | - | - | - | - | 1 |
| Financial Reporting | 1 | - | - | - | - | 1 |
| Fund Balance with Treasury | 1 | - | - | - | - | 1 |
| Order-to-Cash: Accounts Receivable and Revenue | 1 | - | - | - | - | 1 |
| Procure-to-Pay: Accounts Payable and Expenses | 1 | - | - | - | - | 1 |
| Accounting for Long-Term Contracts | - | 1 | - | - | - | 1 |
| Total Material Weaknesses | 6 | 1 | - | - | - | 7 |

| Table 2: Summary of Management Assurances | | | | | | |
|---|---|---|---|---|---|---|
| NDSTF Effectiveness of Internal Controls over Financial Reporting (FMFIA § 2) | | | | | | |
| Statement of Assurance | No Assurance | | | | | |
| Material Weaknesses | Beginning Balance | New | Resolved | Consolidated | Reassessed | Ending Balance |
| Oversight and Monitoring | 1 | - | - | - | - | 1 |
| Financial Reporting | 1 | - | - | - | - | 1 |
| Fund Balance with Treasury | 1 | - | - | - | - | 1 |
| Plan-to-Stock: Inventory | 1 | - | - | - | - | 1 |
| Procure-to-Pay: Accounts Payable and Expenses | 1 | - | - | - | - | 1 |
| Total Material Weaknesses | 5 | - | - | - | - | 5 |

| Table 2: Summary of Management Assurances | | | | | | |
|---|---|---|---|---|---|---|
| DLA Effectiveness of Internal Controls over Operations (FMFIA § 2) | | | | | | |
| Statement of Assurance | No Assurance | | | | | |
| Material Weaknesses | Beginning Balance | New | Resolved | Consolidated | Reassessed | Ending Balance |
| Contract Administration: Nonverification of supplier invoices | 1 | - | 1 | - | - | - |
| Total Material Weaknesses | 1 | - | 1 | - | - | - |

| Table 2: Summary of Management Assurances | | | | | | |
|---|---|---|---|---|---|---|
| DLA Conformance with Federal Financial Management System Requirements (FMFIA § 4) | | | | | | |
| Statement of Assurance | Federal Systems do not conform to financial management system requirements | | | | | |
| Non- Conformances | Beginning Balance | New | Resolved | Consolidated | Reassessed | Ending Balance |
| Security Management | 1 | - | - | - | - | 1 |
| Access Controls | 1 | - | - | - | - | 1 |
| Segregation of Duties | 1 | - | - | - | - | 1 |
| Configuration Management | 1 | - | - | - | - | 1 |
| Total Non-Conformances | 4 | - | - | - | - | 4 |


**Critical Supplies for the Pandemic**

DLA Distribution Process Worker, DLA Distribution Susquehanna, PA, stacks boxes of Ancillary Adult Convenience Kit in preparation of shipment to overseas DoD customers. December 22, 2020. **Photo by** Nutan Chada, DLA Public Affairs

Based on DLA management's analysis of relevant FFMIA compliance indicators available at the time of this report, DLA identified a lack of compliance associated with all three FFMIA Section 803(a) requirements across all funds summarized in the table below.

**Table 2: Summary of Management Assurances**

| Compliance with Section 803(a) of the FFMIA | | |
|---|---|---|
| | Agency | Auditor |
| 1. Federal Financial Management System Requirements | Lack of compliance noted | Lack of compliance noted |
| 2. Applicable Federal Accounting Standards | Lack of compliance noted | Lack of compliance noted |
| 3. USSGL at the Transaction Level | Lack of compliance noted | Lack of compliance noted |

**Helicopter Hoist**

Rhode Island Army National Guardsmen conduct UH-60 Black Hawk helicopter hoist qualification training in West Greenwich, R.I., March 1, 2023. The hoist is used to extract patients in areas that are too small for a helicopter to land.

**Photo by:** Army Officer Candidate Deirdre Salvas

# Revenue Forgone

DLA Energy provides fuel services to both military and public entities. The price for fuel supplied is determined by OUSD(C). Often, DLA Energy prices do not match market prices, and therefore DLA Energy can incur a loss in terms of revenue forgone for a given fiscal year. Revenue forgone denotes the difference between the price DLA charges in exchange transactions and the full cost or market price. DLA Energy's incurred revenue forgone from fuel sales totaled $0 million and $2,589.7 million for the year ended September 30, 2023 and 2022, respectively. The demand for the quantity of petroleum products did not change as a result of the difference in price. While DLA WCF calculates the dollar impact of revenue forgone using the Standard Fuel Price (SFP), certain transactions recorded by DLA use the cost-plus method. Due to DLA WCF's utilization of the cost-plus method, the table below is not a complete depiction of DLA Energy revenue forgone.

In addition, the revenue forgone, disclosed below, is presented on a net basis, but there were instances in FY 2023 where DLA Energy prices did not align with the market prices. However, higher prices based on full cost or market price might reduce the quantity of goods or services demanded and, therefore, the difference between revenue received and such higher prices does not necessarily provide an indication of revenue forgone.

DLA WCF does not track revenue forgone for the SCM and Document Services activity groups. Revenue forgone cannot be quantified due to limitations of financial and non-financial management processes and systems that support the financial statements, as disclosed in DLA WCF, GF, and NDSTF Note 1.B., *Basis of Presentation and Accounting*.

## DLA Energy Revenue Forgone

(dollars in millions)

| | FY 2023 | FY 2022 | FY 2021 | FY 2020 | FY 2019 |
|---|---|---|---|---|---|
| Energy Revenue Forgone | - | $ (2,590) | $ (810) | - | - |
| Total Revenue Forgone | - | $ (2,590) | $ (810) | - | - |

**Pride in Painting**

Jody Lindsey, Painter, DLA Aviation Industrial Plant Equipment Services Division, is painting this Horizontal Boring Machine for a Navy Puget Sound customer. April 19, 2022. Photo taken by Nutan Chada, DLA Public Affairs. **Photo by:** Courtesy of DLA

# Management Challenges

DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD
FORT BELVOIR, VIRGINIA 22060-6221

July 19, 2023

MEMORANDUM FOR VICE ADMIRAL MICHELLE C. SKUBIC, DIRECTOR, DLA

SUBJECT: Major Management and Performance Challenges Facing the Defense Logistics Agency

This year the Office of the Inspector General (OIG) has aggregated the major management and performance challenges facing DLA into three general topics: Business Process Documentation and Internal Controls, Data Management, and Property Accountability. We also identified two risks that were not related to one of the forementioned consolidated risk topics. The general risk topics are discussed below.

**Business Process Documentation and Internal Controls:** This area highlights the need for adequate business process documentation, internal controls, and complementary user entity controls for all DLAs business processes. DLA OIG is in the process of completing a series of projects reviewing the steps taken to ensure that DLA obtains an unmodified opinion on all its financial statements. Generally, we are finding that the basic, foundational business process and internal control documentation is inadequate or non-existent.

**a. Audit Documentation:** DLA OIG is in the process of completing a series of projects reviewing the steps taken to ensure DLA obtains an unqualified opinion to confirm our financial statements are fair and appropriately represented. Generally, we are finding that the basic, foundational business process and internal control documentation is missing. In 2022 we documented this challenge as DLA attempted to minimize the number of future notices of finding and recommendation (NFR) from our public accountant, as well as address existing NFRs. We have not seen sufficient progress on this risk. Without accurate and detailed business process flowcharts and descriptions (including formal policy and implementing procedures), external auditors cannot quickly and easily understand the process and DLA cannot prove that the correct internal controls have been developed. Business process documentation must address inputs received from other processes, identification of risks associated with a process, management's evaluation and/or acceptance or addressing of the risk, the implementation of associated internal controls, and the output(s) to other business processes. Until this is achieved, DLA will continue receiving numerous NFRs and the external auditor will continue to deem corrective actions inadequate.

**b. Sales of DoD Property:** DLA still needs to establish sufficient policy and oversight of DLA sales of property in policy. This concern was formally recognized in a finding in FY18 during an Agency Management Review and has not been corrected to date. While multiple components of DLA are involved in the sales of DoD property, DLA Headquarters has limited expertise within the staff to develop adequate policy. Additionally, sales procedures and process are impacted by law and rules from several governmental agencies. Inadequate agency and MSC policy and the lack of execution oversight by DLA remains an area of risk that requires mitigation and remediation and clear documentation in the business process.

**Data Management:** The need for DLA to begin using the significant amount of data that exists within the data warehouse to make appropriate inventory purchase and stockage decisions go hand in hand with business process documentation and internal controls management. Specifically highlighting the risk of single point of failure and just-in-time inventory.

**a. Supply Chain Security and Risk Management:** DLA needs to continually evaluate our supply chains for single-point failures to prevent disruptions to DLA's Warfighter and Whole of Government customers. This challenge highlights the lack of domestically based integrated supply chains, as well as other risks in DLA's reliance on the Defense industrial base. These Defense industrial base risks should be addressed in business process documentation so Congress can address or accept the risk.

**b. Just-In-Time Inventory:** Good data management can help mitigate the dependency of just in-time inventory management after the recent years of underfunding for cost-savings.

**Property Accountability:** As previously disclosed in both past management challenge letters as well as in audit and inspection work there are six accountability risks. The five detailed risks are: lack of advance shipment notices, imbalance in materiel availability, contractor non-compliance, supply discrepancy reports, and financial liability investigations. All five of these risks could adversely affect the material available to Warfighters and whole of government customers. These risks cover the entire property accountability process and should have been previously identified in an "end-to-end" process map.

**a. Suspended Inventory:** The lack of system generated Advanced Shipping Notice (ASN) and Pre-Positioned Materiel Receipts (PMR) are causing significant suspended inventory at the DLA Distribution warehouses that receive this material. If a warehouse worker cannot quickly identify the shipping details associated with a shipment, the material risks being suspended for additional research. While this material is being researched, it is not available for shipment to customers. DLA Distribution has identified that about 90 percent of the material without advance shipment details is owned by the Services. Failure to provide advance shipment details leads not only to additional research, but potential receipt of materiel under the wrong owner which leads to improper billing, adjustments, delays in vendor reimbursement, and materiel non-availability leading to rebuys across the Department. Currently there is over $4 billion is suspended stock, which also adversely impacts the Departments ability to earn an unqualified audit opinion.

**b. Material Availability:** DLA incurs substantive risk due to an imbalance between DoD resourced Materiel Availability (MA) (targeting 85% within the range of 82 to 89%) and the expectation by the Military Services for MA performance of 90% and higher. This disconnection manifests as shortfalls in materiel availability. DLA can align to the DoD-directed MA so long as customer demand supports the higher MA or a financing strategy is pursued (e.g., cash infusion or surcharge when expanding inventories). While DLA is working to align customer performance expectations with its resourcing profile, this remains a significant risk to effective operations and adequate funding within the Working Capital Fund.

**c. Contracting Officer's Representatives:** This area was identified in FY20 and remains on the list because of significant concerns about the quality of Contracting Officer's Representatives' (COR) work. Previous audit work identified that COR files did not contain adequate evidence to support monitoring of contractors. Given the significant number of DLA contracts, to improve fiscal stewardship, it is essential to improve COR performance and quality of work.

**d. Supply Discrepancy Reports:** When non-compliant materiel is received DLA Distribution must initiate Supply Discrepancy Reports (SDRs). Materiel is primarily suspended for labeling, packaging, packing, and preservation, which negatively impacts customer readiness and DLA cash flow. The cost to DLA for research and legal actions if litigation is required is increasing exponentially. Additionally, downstream impacts include maintaining additional facilities, materiel handling equipment, and FTEs to manage this materiel.

3

**e. Financial Liability Investigation Reports:** Based on numerous OIG investigations, financial liability investigations of property loss were inadequate and failed to hold responsible officials accountable for failure to maintain accountability of property under their control.

We also identified two risks (ongoing contingency operations and rare earth elements) that were not related to one of the three general risk topics. The first risk is contingency operations are placing greater stress on the logistics supply system, especially for legacy systems that are only in minimal quantities across DoD. The second risk is DLA stores bulk, unrefined rare earth elements through the DLA Transaction Fund as directed by Congress. While DLA only purchases, stores, and accounts for this material, we recognize that the capacity of the Defense domestic industrial base to refine and move this material into end products may be limited. Mitigating this risk may require DLA or DoD to incentivize the Defense domestic industrial base sustainment in refinery capabilities.

In 2024 the DLA OIG will focus on improving the foundational business process and internal control documentation to assist DLA in preparing for ongoing financial audits. It is critical for DLA leadership to be aware of these challenges as they relate directly to ongoing/future financial audits, providing the best value to the taxpayer, and the best support to the warfighter. Addressing each of these risk challenges will improve DLA's internal control structure and thereby help the organization achieve unmodified financial statement opinions that conclude DLA's financial statements are presented fairly, complete and accurate in all material respects, in accordance with the applicable financial reporting framework.

Please contact Mr. Steven Pigott, Deputy Inspector General for Internal Audit, if you would like to further discuss the risks present in this memorandum. Mr. Pigott can be reached at 571-767-6282 or Steven.Pigott@dla.mil.

WILLIAM A. RIGBY
Inspector General

# Payment Integrity

The Payment Integrity Information Act of 2019 (PIIA) (Pub. L.116-117), requires agencies to review and assess all programs and activities they administer and identify those determined to be susceptible to significant improper payments (IPs), estimate the annual amount of IPs, and submit those estimates to Congress. In accordance with DoD 7000.14-R FMR, Volume 4, Chapter 14, Improper Payments, DoD components that entitle (i.e. process or compute) payments conduct risk assessments of their payment processes and random post-payment reviews to estimate IPs.

The OUSD(C) Accounting & Finance Policy Directorate (A&FP) compiles the Department-wide results annually as part of DoD's AFR. As DLA's Service Provider, DFAS entitles payments and provides the results of post-payment reviews to OUSD(C) A&FP on behalf of its customers. OMB Circular A-123, Appendix C defines an IP as any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements. It includes duplicate payments, any payment made to an ineligible recipient, any payment for an ineligible good or service, any payment for a good or service not received (except for such payments where authorized by law), and any payment that does not account for credit for applicable discounts.

In accordance with OMB Circular A-136 Section II.4.5 and PIIA, each Executive Branch agency must complete the Annual Data Call issued by OMB and provide a link to PaymentAccuracy.gov in their AFR or Performance and Accountability Reports (PARs) to fulfill reporting requirements. In addition, each Executive Branch agency should report on the actions taken in their AFR or PAR.

For detailed reporting on DoD payment integrity, refer to the OI section of the consolidated DoD AFR at: https://comptroller.defense.gov/odcfo/afr/.

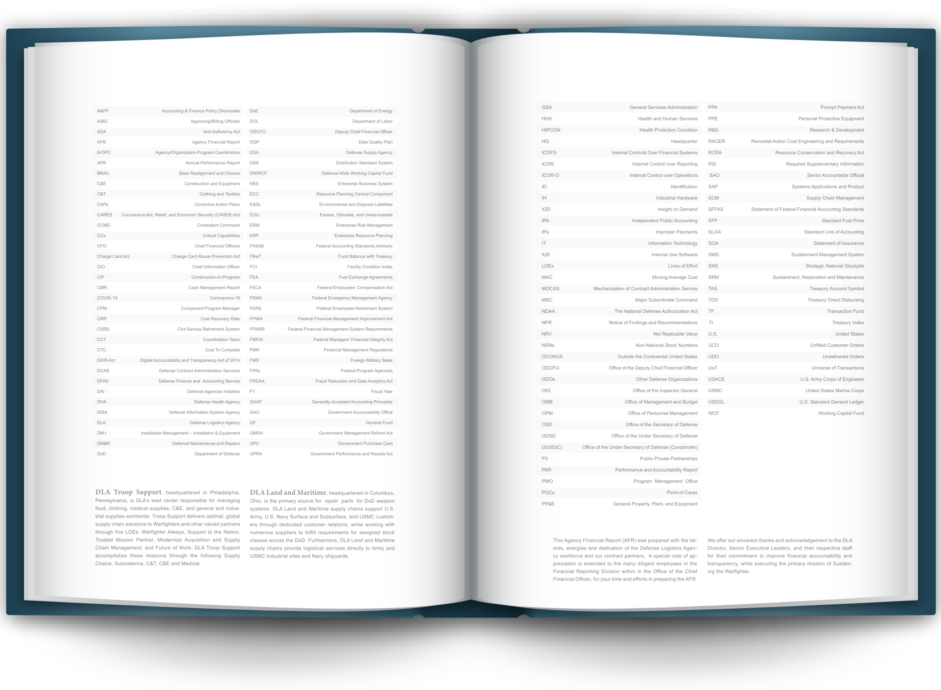
**DLA Contingency Team at Eagle Rising 2.0**

DLA Distribution Expeditionary leaders meet with DLA Information Operations Contingency team during the DLA FEMA Eagle Rising 2.0 exercise, April 20, 2022, at Joint Base MacGuire-Dix-Lakehurst in New Jersey. Photo by Nutan Chada, DLA Public Affairs.

**Photo by:** DLA

# Appendix

# A & B



## Group Boarding

Soldiers board an Air Force C-130 Hercules alongside Italian troops at Aviano Air Base, Italy, Jan. 26, 2023.

**Photo By:** Army Cpl. Genesis Miranda

# Appendix A:
# J/D Codes, DLA HQ Program Support Structure, Roles and Responsibilities

The following are DLA Enterprise-wide J/D Codes and DLA HQ Program Support Structures:

**DLA Human Resources (J1)** provides the full range of human resource services to include Operational, Human Performance, Talent Management, Performance Management, Labor Relations and Human Resources Policy for the DLA workforce. DLA Human Resources recruits, hires, trains, and sustains a mission-ready workforce for DLA and Human Resources customers, using world-class policies, processes, programs, and tools.

**DLA Logistics Operations (J3)** is responsible for the end-to-end supply chain management of DLA's supply chains, providing logistics and material process management policy, guidance, and oversight. J3 integrates strategic, operational, and tactical perspectives, as well as commands and controls functions for contingency operations and logistics supply chain planning. J3 maximizes the readiness and logistics combat power by leveraging enterprise solutions to support DLA's global customer base.

**DLA Information Operations (J6)** as DLA's knowledge broker, provides comprehensive, best practice IT support to the DoD/DLA Logistics Business Community, resulting in customer support; efficient and economical computing; data management; electronic business; telecommunication services; key management; and secure voice systems for DoD, DLA, and geographically separated operating locations. The Director of Information Operations serves as DLA's CIO. DLA Information Operations also manages DLA's R&D IT program.

**DLA Acquisition (J7)** 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 of DLA Acquisition also serves as the Agency's Component Acquisition Executive. DLA Acquisition provides oversight of DLA Contracting Services Office.

**DLA Finance (J8)** is responsible for obtaining and allocating resources; analyzing execution; and providing fiscal guidance and advice to support the Agency, its business areas, and its MSCs in accomplishing DLA's mission. DLA Finance prepares the AFRs and guides DLA in its Audit Remediation efforts. The Director of Finance also serves as DLA's CFO.

**DLA Joint Reserve Force (J9)** provides DLA with trained, ready, and available reservists from the Army, Air Force, Navy, and Marine Corps for worldwide contingency operations and support of ongoing operations, surge requirements, and logistics planning.

**DLA Office Of Small Business Programs (DB)** provides small business advocacy and promotes small business utilization to strengthen the competency, capability, and commitment of the industrial base that fulfills DLA's mission as the Nation's Combat Logistics Support Agency. DLA Office of Small Business Programs is responsible for implementation of the Procurement Technical Assistance Program to expand the number of businesses capable of participating in contracts with DoD, other Federal agencies, state and local governments, and government prime contractors.

**DLA General Counsel (DG)** delivers professional, candid, and independent legal advice and services to DLA.

**DLA Command Chaplain (DH)** serves as the program manager for religious support logistics. This office provides the DLA Director and the staff a clear picture of workforce morale as affected by religion, ensuring the free exercise of religion to support the Warfighter and the employees in the workplace at DLA.

**DLA Installation Management (DM)** provides enterprise-wide Agency policy, program, and worldwide operational support in environmental management; safety and occupational health; installation management; public safety; forms and policy management; and morale, welfare, and recreation for DLA.

**DLA Equal Employment Opportunity And Diversity Office (DO)** provides DLA senior leadership, staff, and subordinate commands enterprise-wide respondent and subject matter expertise on all Equal Employment Opportunity Compliance oversight, Affirmative Employment and Diversity and Inclusion.

**DLA Public Affairs (DP)** provides public affairs support, communication strategy development, and engagement guidance to DLA senior leadership, staff, and subordinate commands. The DLA Public Affairs office develops and administers internal news and information; manages DLA social media and public engagement policies; and develops programs that communicate DLA's role as a Combat Support Agency that adds value to the Defense Department, military services, CCMDs and the American people.

**DLA Transformation (DT)** directorate synchronizes strategy, policy, and process to support the Warfighter, strengthen alliances and drive innovation. DT manages DLA's strategic plan, executive governance forums, and the agency-wide deployment of Enterprise Process Management, Continuous Process Improvement, Enterprise Organizational Alignment, and Enterprise Policy Management programs.

**DLA Office Of The Inspector General (OIG)** coordinates and synchronizes GAO and Department of Defense Office of Inspector General (DoDIG) audits with all DLA components; tracking, monitoring, and assessing the implementation of audit corrective actions and communicating completion results. They sustain strategic engagement with the Defense Counsel on Integrity and Efficiency and their subcommittees, as well as relationships with DoDIG Criminal Investigative Services, Military Criminal Investigation Services, and other Law Enforcement Agencies. DLA OIG also conducts administrative investigations and crime vulnerability assessments that align with Agency risks and strategic goals. The DLA OIG internal audit plan is derived from DLA's ERM efforts, and also encompasses external audit projects derived from GAO's high-risk list.

# DLA Major Subordinate Commands

The following are DLA WCF MSCs:

**DLA Troop Support**, headquartered in Philadelphia, Pennsylvania, is DLA's lead center responsible for managing food, clothing, medical supplies, C&E, and general and industrial supplies worldwide. Troop Support delivers optimal, global supply chain solutions to Warfighters and other valued partners through five LOEs: Warfighter Always, Support to the Nation, Trusted Mission Partner, Modernize Acquisition and Supply Chain Management, and Future of Work. DLA Troop Support accomplishes these missions through the following Supply Chains: Subsistence, C&T, C&E and Medical.

**DLA Land And Maritime**, headquartered in Columbus, Ohio, is the primary source for repair parts for DoD weapon systems. DLA Land and Maritime supply chains support U.S. Army, U.S. Navy Surface and Subsurface, and USMC customers through dedicated customer relations, while working with numerous suppliers to fulfill requirements for assigned stock classes across the DoD. Furthermore, DLA Land and Maritime supply chains provide logistical services directly to Army and USMC industrial sites and Navy shipyards.

**Manning the Rails**
Sailors man the rails aboard the USS Roosevelt as the ship returns from patrol to Naval Station Rota, Spain, Feb. 4, 2023. Roosevelt completed her fourth patrol in the U.S. Naval Forces Europe area of operations. **Photo By:** Navy Petty Officer 2nd Class Danielle Baker

major weapon systems. The DLA Aviation supply chain provides mapping, kitting, chemical, petroleum packaging, gases, and cylinder items to the military services. In addition, DLA Aviation provides engineering, sustainability, ozone depleting substances reserve, and industrial plant equipment services.

**DLA Distribution**, headquartered in New Cumberland, Pennsylvania, is responsible for the receipt, storage, issuance, packing, preservation, and transportation of items worldwide. It operates a network of distribution centers around the world that provide timely and quality support to the Warfighters. Their Global Stock Position Plan ensures rapid distribution of critical military items. DLA Distribution's overseas distribution operations are located in Europe, Middle East, and Pacific Asia regions.

- Selling petroleum and aerospace fuels
- Arranging for petroleum support services
- Providing facility/equipment maintenance on fuel infrastructure
- Performing energy-related environmental assessment and cleanup
- Storing and transporting for bulk and aerospace products, and Performing quality functions for petroleum in support of the military services, as well as for the privatization of their utility systems
- Providing Installation Energy products and Utility Services

**DLA Disposition Services**, headquartered in Battle Creek, Michigan, receives EOU DoD property and provides ultimate disposal services through reutilization, transfer, donation, and sales. Property not reutilized within DoD is available for transfer to other Federal agencies or for donation to authorized non- profit organizations or state and local governments. Property not reused, transferred, or donated is either competitively sold or disposed of in an environmentally safe manner. DLA Disposition Services also arranges for the worldwide disposal of hazardous waste in compliance with laws and regulations.

**The Training Trio**

The USNS Laramie supplies fuel to the USS Bataan and USS Carter Hall during amphibious squadron/Marine expeditionary unit integration training in waters off North Carolina, Jan. 31, 2023. **Photo By:** Marine Corps Cpl. Michele Clarke

# Appendix B: Abbreviations & Acronyms

| | | | |
|---|---|---|---|
| A&FP | Accounting & Finance Policy Directorate | DoE | Department of Energy |
| A/BO | Approving/Billing Officials | DOL | Department of Labor |
| ADA | Anti-Deficiency Act | DQP | Data Quality Plan |
| AFR | Agency Financial Report | DSA | Defense Supply Agency |
| A/OPC | Agency/Organization Program Coordinators | DWWCF | Defense-Wide Working Capital Fund |
| APR | Annual Performance Report | EBS | Enterprise Business System |
| ASIC | Application Specific Integrated Circuit | ECC | Resource Planning Central Component |
| ASP | Annual Sales Plan | E&DL | Environmental and Disposal Liabilities |
| BRAC | Base Realignment and Closure | EOU | Excess, Obsolete, and Unserviceable |
| C&E | Construction and Equipment | ERM | Enterprise Risk Management |
| C&T | Clothing and Textiles | ERP | Enterprise Resource Planning |
| CAPs | Corrective Action Plans | FASAB | Federal Accounting Standards Advisory Board |
| CARS | Central Accounting and Reporting System | FBwT | Fund Balance with Treasury |
| CCMD | Combatant Command | FCI | Facility Condition Index |
| CCs | Critical Capabilities | FEA | Fuel Exchange Agreements |
| CFO | Chief Financial Officers | FECA | Federal Employees' Compensation Act |
| Charge Card Act | Charge Card Abuse Prevention Act | FEMA | Federal Emergency Management Agency |
| CIP | Construction-in-Progress | FERS | Federal Employees Retirement System |
| CMR | Cash Management Report | FFMIA | Federal Financial Management Improvement Act |
| COLA | Cost of Living Adjustments | FFMSR | Federal Financial Management System Requirements |
| COVID-19 | Coronavirus-19 | FMFIA | Federal Managers' Financial Integrity Act |
| CPM | Component Program Manager | FMR | Financial Management Regulations |
| CRR | Cost Recovery Rate | FMS | Foreign Military Sales |
| CSRS | Civil Service Retirement System | FY | Fiscal Year |
| CTC | Cost To Complete | GAAP | Generally Accepted Accounting Principles |
| DATA Act | Digital Accountability and Transparency Act of 2014 | GAO | Government Accountability Office |
| DERP | Defense Environmental Restoration Program | GF | General Fund |
| DFAS | Defense Finance and Accounting Service | GMRA | Government Management Reform Act |
| DAI | Defense Agencies Initiative | GPC | Government Purchase Card |
| DISA | Defense Information System Agency | GPRA | Government Performance and Results Act |
| DLA | Defense Logistics Agency | GSA | General Services Administration |
| DM-I | Installation Management – Installation & Equipment | HHS | Health and Human Services |
| DM&R | Deferred Maintenance and Repairs | HQ | Headquarter |
| DoD | Department of Defense | ICOFS | Internal Controls Over Financial Systems |

| | |
|---|---|
| ICOFR | Internal Controls over Financial Reporting |
| ICOR-O | Internal Controls over Operations |
| ID | Identification |
| IH | Industrial Hardware |
| IOD | Insight on Demand |
| IPA | Independent Public Accounting |
| IPs | Improper Payments |
| IT | Information Technology |
| IUS | Internal Use Software |
| LOEs | Lines of Effort |
| MAC | Moving Average Cost |
| MOCAS | Mechanization of Contract Administration Services |
| MSC | Major Subordinate Command |
| NDAA | The National Defense Authorization Act |
| NDSTF | National Defense Stockpile Transaction Fund |
| NFR | Notice of Findings and Recommendations |
| NRV | Net Realizable Value |
| NSNs | Non-National Stock Numbers |
| O&M | Operation and Maintenance |
| OCONUS | Outside the Continental United States |
| ODOs | Other Defense Organizations |
| OIG | Office of the Inspector General |
| OMB | Office of Management and Budget |
| OPM | Office of Personnel Management |
| OSD | Office of the Secretary of Defense |
| OUSD | Office of the Under Secretary of Defense |
| OUSD(C) | Office of the Under Secretary of Defense (Comptroller) |
| P3 | Public-Private Partnerships |
| PAR | Performance and Accountability Report |
| PDW | Procurement Defense-Wide |
| POCs | Point-of-Cares |
| PP&E | General Property, Plant, and Equipment |
| PPA | Prompt Payment Act |
| PPE | Personal Protective Equipment |
| R&D | Research & Development |
| RACER | Remedial Action Cost Engineering and Requirements |
| RCRA | Resource Conservation and Recovery Act |
| RSI | Required Supplementary Information |
| SAP | Systems Applications and Product |
| SCM | Supply Chain Management |
| SFFAS | Statement of Federal Financial Accounting Standards |
| SFP | Standard Fuel Price |
| SLOA | Standard Line of Accounting |
| SMS | Sustainment Management System |
| SNS | Strategic National Stockpile |
| SRM | Sustainment, Restoration and Maintenance |
| TAS | Treasury Account Symbol |
| TDD | Treasury Direct Disbursing |
| TFM | Treasury Financial Manual |
| TI | Treasury Index |
| U.S. | United States |
| UCO | Unfilled Customer Orders |
| UDO | Undelivered Orders |
| UoT | Universe of Transactions |
| USACE | U.S. Army Corps of Engineers |
| USMC | United States Marine Corps |
| USSGL | U.S. Standard General Ledger |
| WCF | Working Capital Fund |

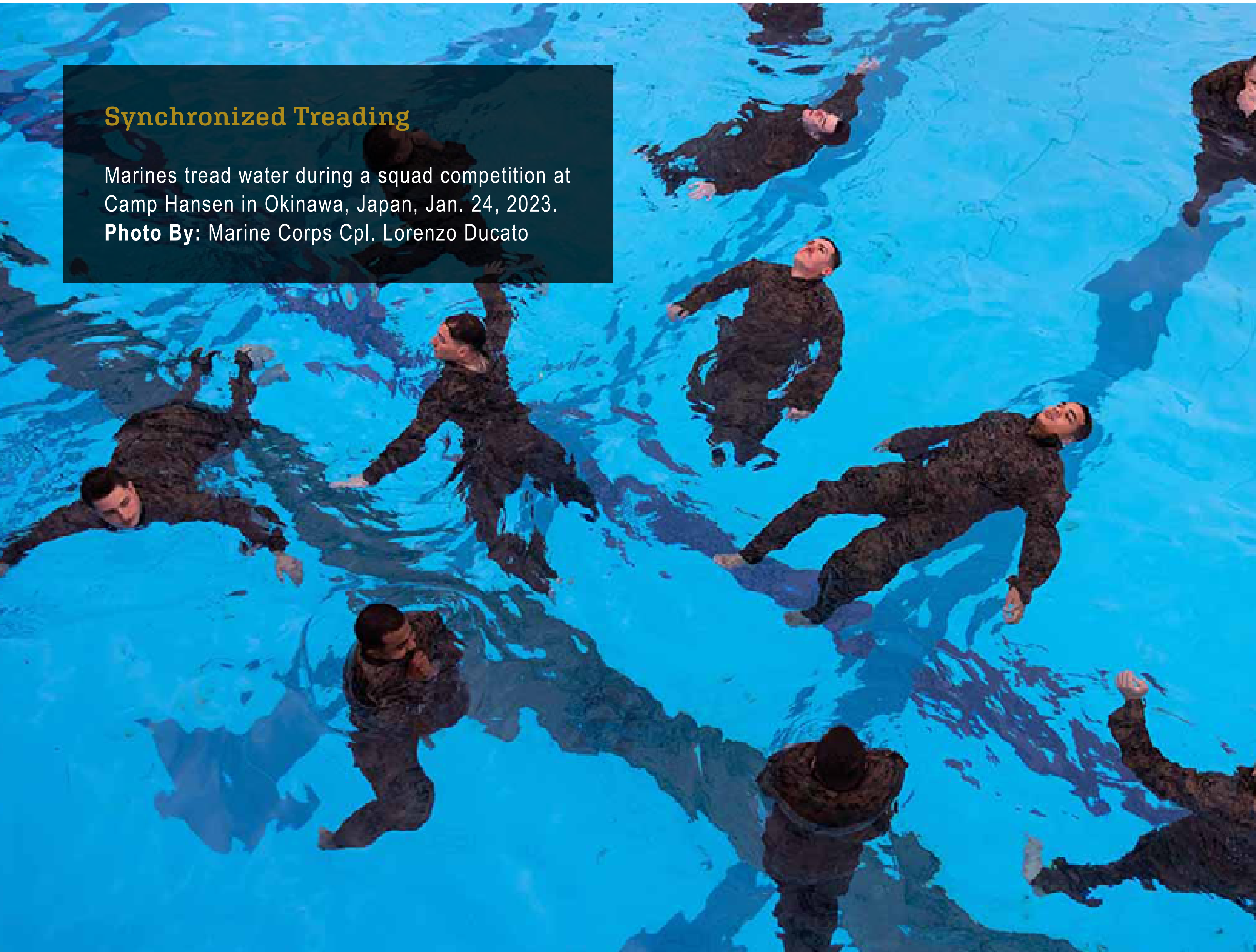
# Acknowledgments

This AFR was prepared with the talents, energies and dedication of the Defense Logistics Agency workforce and our contract partners.  A special note of appreciation is extended to the many diligent employees in the Financial Reporting Division within the Office of the Chief Financial Officer for your time and efforts in preparing the AFR.

We offer our sincerest thanks and acknowledgement to the DLA Director, Senior Executive Leaders, and their respective staff for their commitment to improve financial accountability and transparency, while executing the primary mission of Sustaining the Warfighter.

Icon design courtesy of Sahab Uddin, Gregor Cresnar, Made x Made and Vectors Point from **Noun Project**.

Images courtesy of **DoD**, **DLA**, **Freepik** and **Unsplash.**



## Synchronized Treading

Marines tread water during a squad competition at Camp Hansen in Okinawa, Japan, Jan. 24, 2023.
**Photo By:** Marine Corps Cpl. Lorenzo Ducato

Warfighter Always!

The Nation's Logistics Combat Support Agency

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