



Department of the Navy

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

**Real Property, Plant & Equipment
(PP&E)**

Personal Property

**Operating Materials & Supplies
(OM&S) and**

Military Equipment:

A Common Thread

**Personal Property
Management Conference
12-14 Aug 2003**



- ◆ The Audit Opinion
- ◆ Applicable Standards and Reporting Requirements
- ◆ Real PP&E -- Issues
- ◆ Personal Property -- Issues
- ◆ OM&S -- Issues
- ◆ Military Property-- Issues
- ◆ Summary



What are Audit Opinions?

- ◆ Auditors express an independent opinion that the financial statements are fairly presented per accounting standards.
 - Unqualified: “clean opinion.”
 - Qualified: fairly presented with certain material exceptions.
 - Adverse: not fairly presented.
 - Disclaimer: auditors were unable to form an opinion on the fairness of the financial statements.



What are Auditable Financial Statements?

- ◆ Financial statements on which the auditors can express an opinion.
- ◆ Auditors form an opinion by testing five management assertions:
 - Existence or Occurrence
 - Completeness
 - Rights and Obligations
 - Valuation or Allocation
 - Presentation and Disclosure
- ◆ Documentation: Audit Ready Format





Applicable Standards and Requirements

- ◆ Statement of Federal Financial Accounting Standards (SFFAS) No. 3, “Accounting for Inventory and Related Property”
- ◆ SFFAS No. 6, “PP&E”
- ◆ SFFAS No. 10, “Internal Use Software”
- ◆ SFFAS No. 23, “Eliminating the Category National Defense PP&E”
- ◆ DoDFMR Vol 4, Ch 4, “OM&S”
- ◆ DoDFMR Vol 4, Ch 6, “PP&E”
- ◆ DoDFMR Vol 6B, Form and Content
- ◆ DON implementing guidance



Real Property, Plant and Equipment

◆ Real Property

- Tangible assets that have useful lives of 2 or more years
- Not intended for sale in the ordinary course of operations
- Acquired or constructed with the intention of being used or being available for use by the entity

◆ Classes of Real Property-- Land, Buildings, Structures, and Utilities and Leasehold Improvements

◆ Existence and Completeness of DON Real PP&E should pass the test.



Real Property, Plant and Equipment

- ◆ DON has acceptable values for Real Property with the exception of Leasehold Improvements
- ◆ Issue: Leasehold Improvements meeting the capitalization threshold are not being reported
 - Commands to review and identify leasehold improvements and develop a methodology for tracking them
- ◆ The source of capitalized assets acquired from other federal sources is not being identified
 - Retrieve capitalized assets acquired from other federal sources
- ◆ DON's Real Property System, Internet Naval Facility Asset Data Store (iNFADS) does not interface with the accounting system
 - Develop an interface between iNFADS and the accounting system



- ◆ Completed deployment of the Defense Property Accountability System (DPAS) throughout the DON General Funded Commands/Activities during FY 2002.
- ◆ Some areas not included in DPAS
 - Considered NDPP&E at the time of deploying DPAS
 - Now will be considered under the Military Equipment effort
- ◆ Internal Use Software may be materially understated
 - Commands need to review the guidance and capture data in DPAS
- ◆ Trading Partner information for transfers in/out to government agencies -- needs to be captured and reported



General PP&E, Note 10

Note 10. General Property, Plant, and Equipment (PP&E) (Net)

As of September 30,	2002					2001
	Depreciation/ Amortization Method	Service Life In Years	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior Year Net Book Value
(Amounts in thousands)						
1. Major Asset Classes:						
A Land	NA	NA	\$ 645,924	NA	\$ 645,924	\$ 655,751
B Buildings, Structures, And Facilities	SL	20-40	32,862,380	\$(12,612,305)	20,250,075	19,483,307
C Leasehold Improvements	SL	Lease Term	0	0	0	0
D Software	SL	2,5 or 10	1,059	(423)	636	1,067
E Equipment	SL	5 Or 10	2,837,863	(1,993,072)	844,791	916,938
F. Military Equipment	Composite/ Group	Varied	0	0	0	0
G Assets Under Capital Lease ¹	SL	Lease Term	1,116	(206)	910	7,153
H Construction/Work-in- Progress	NA	NA	4,367,101	NA	4,367,101	3,896,679
I. Other						592
J. Total General PP&E			\$ 40,715,443	\$(14,606,006)	\$ 26,109,437	\$ 24,961,487



Operating Materials & Supplies (OM&S)

- ◆ OM&S-- consists of tangible personal property to be consumed in normal operations
- ◆ Recognition
 - Consumption method-- recognized as an asset upon purchase and expensed when issued to the “end user” for consumption in normal operations.
 - Purchases method-- OM&S expensed when purchased.
- ◆ “End User”-- any component of a reporting entity that obtains goods for direct use in the component’s normal operations
- ◆ Valuation-- OM&S shall be valued at historical cost



Total Reported Value of OM&S, FY 2002

Principal End Items	\$ 10,317,471	AEMS, SPAWARSCOM, UDAPS, FMO
Sponsored Owned Material	9,814,710	GOLD, ILSMIS, SYMIS, SPAWARSCOM, FMO
Ammunition and Munitions	9,659,749	MAARS II, CAIMS
APA Secondary Items	1,654,127	MFCS, ATLASS, ATLASS II, SASSY, FMO
Residual Assets	1,288,052	RRAM
Other	269,486	BUMED, COMLANFLT, FMO
	\$33,003,595	



Deficiencies

1. The universe of OM&S is not verifiable.
2. Inventory valuation does not meet federal accounting standards.
3. Classification of elements of OM&S is not in accord with established standards.
4. Government Furnished Material (GFM) and Contractor Acquired Material (CAM) are generally not included in the OM&S values reported.
5. Trading partner information is not available for reporting of transfers in / transfers out.
6. Lack of internal controls over in-transit items.
7. Systems are not compliant.



- ◆ Universe of OM&S is not verifiable
 - ◆ Key audit element
 - ◆ What's on the shelf is in your books
 - ◆ What's in your books is on your shelf
 - ◆ Review physical inventory procedures
 - ◆ Are they timely?
 - ◆ Are they complete?
 - ◆ Are the results good?
 - ◆ Determine delta resources needed to sustain a timely and sound physical inventory program



Valuation: Prerequisites for Auditability

- ◆ *Establish* historical cost valuation baseline for each item of OM&S
 - Baseline as of 1 Oct 2003 for Qualified Opinion
 - Best method based upon available data
 - Must be supportable and auditable
- ◆ *Maintain* historical cost valuation
 - Recalculate MAC based upon purchase receipts
 - Audit trail from 1 Oct 2003 to 30 Sep 2004
 - Must be transaction based/derived



- ◆ Based on existing data, processes and systems
- ◆ Follow prescribed accounting standards
- ◆ Valuation methods may include Latest Acquisition Cost (LAC), First In First Out (FIFO) or other historical methods
 - Reflective of items in inventory
 - Need for sustainability
 - Simplest, easiest, but sound in application
- ◆ Method must be auditable



Maintaining Moving Average Cost (MAC) Valuation

- ◆ MAC is the DoD approved valuation for historical cost (OUSD(C) memo of 6 Jul 01)
 - MAC will be applied to all like units held regardless of condition code
 - MAC will be applied to units acquired through donation, monetary or non-monetary exchange, return from end-use, gains/losses, transfers, etc.
- ◆ MAC calculation:
 - Triggered based upon a receipt from procurement
 - $$\frac{(\text{units on-hand} \times \text{MAC}) + (\text{units received} \times \text{cost of units})}{\text{units on-hand} + \text{units received}}$$



Valuation: From Logistics to Accounting

- | | | |
|--|-----|--|
| ◆ 1511
Held for
Use | ■ A | Issuable Without Qualification |
| | ■ B | Issuable With Qualification |
| | ■ C | Priority Issue |
| | ■ D | Test/Modification |
| ◆ 1514
Held for
Repair | ■ E | Reparable |
| | ■ F | Reparable |
| | ■ G | Incomplete |
| | ■ L | Suspended (In Litigation) |
| | ■ M | Suspended (In Work) |
| | ■ Q | Suspended (Quality Deficient Exhibits) |
| ◆ 1513 Excess,
Obsolete,
Unserviceable | ■ R | Suspended (Reclaimed Items, Awaiting
Condition Determination) |
| | ■ H | Condemned |
| | ■ P | Reclamation |
| | ■ S | Scrap |
| | ■ V | Condemned Ammunition |



Valuation Defined by USSGL Line Item

- ◆ OM&S Held for Use (USSGL 1511)
 - Valued at MAC
 - Contains values for items with condition codes A through D
- ◆ OM&S Held for Future Use (USSGL 1512)
 - Not used by DoD
 - No management codes or financial valuation distinction between “Future Use” and “Use” to support populating this account on a transactional basis



Valuation Defined by USSGL Line Item (cont.)

◆ OM&S Held for Repair (USSGL 1514)

- Valued at MAC
- Offset by an allowance account (USSGL 1519) for impairment
- Contains values for items with condition codes
 - E & F - Repairable
 - G - Incomplete
 - L, M, Q & R - Suspended (various reasons)
- MAC less allowance equals impaired value

◆ Allowance for Impairment (Repair) (USSGL 1519)

- Valued as a percentage of MAC
- Based upon a sampling of items having recent repair and purchase costs



Valuation Defined by USSGL Line Item (cont.)

- ◆ OM&S-Excess, Obsolete, & Beyond Repair (SGL 1513)
 - Valued at MAC
 - Offset by an allowance account (USSGL 1519) for condemnation
 - No management codes to distinguish between excess and obsolete material and “Held for Repair” and “Use” to support transactional posting
 - Contains values for items with condition codes
 - H, P, S, V - Condemned, Reclamation, Scrap & Condemned
 - MAC less allowance equals condemned value
- ◆ Allowance for Condemnation (USSGL 1519)
 - Valued as 100 percent of MAC



- ◆ Many “sources/classes” for OM&S amounts
 - “Sponsor-owned material
 - “Cognizance Symbol” material
 - “APA Secondary Item” material
 - “APA Principal Item” material
 - “Residual” material
- ◆ Is it OM&S?
 - Sources may contain a mix of asset types
 - New category of assets - Military Equipment
- ◆ Resource implications of modifying reporting



- ◆ Concern whether GFM and CAM is reported
 - If yes, is it auditable, valid
 - If no, should it be
- ◆ Where should it be captured?
 - In government systems via contractor reports
 - From contractor systems
- ◆ Are GFM and CAM assets properly categorized?
 - Could it support Military Equipment, and be W-I-P
- ◆ What is cost of answer?



- ◆ Historically difficult to “manage”
- ◆ Subject to continued audit scrutiny
- ◆ Intransit types
 - From procurement (FOB origin)
 - Between accountable officers
 - Repairable exchange process (carcass returns)
- ◆ Potential for duplicate reporting
 - Receiving activity reports as “on-hand”
 - Sending activity continues to report as “intransit”
- ◆ Cost of auditable management?



- ◆ Beginning with FY 1998, acquisition costs for items classified as National Defense Property, Plant, and Equipment (NDPP&E) were removed from the Balance Sheet and expensed in the period incurred.
- ◆ The Federal Accounting Standards Advisory Board (FASAB) issued SFFAS No. 23 that requires “full” cost of these assets be capitalized and depreciated beginning with FY 2003.
 - Existing equipment must be valued
 - In-process acquisitions must be valued
 - Depreciation must be reported
- ◆ SFFAS No. 23 allows for development of historical costs for existing assets using various estimating techniques (budget, engineering documents, other reports).



- ◆ During FY 2002, completed valuation of three pilot programs. (DDG 51; Paladin; F-15)
 - Purpose: to develop process and business rules.
- ◆ For FY 2003, using a parametric estimate for the value and depreciation of military equipment for FY 03 reporting.
- ◆ Conduct additional pilots within DON (NAVAIR, Marine Corps, SSP, and SPAWAR)
- ◆ Determine the “Universe” of Military Equipment
 - FY 1972-2009 P-1 list
 - Extracts from various accountability systems
- ◆ Value the “Universe” of Military Equipment



◆ Vision

- Work with appropriate Business Enterprise Architecture (BEA) Domain Owners

- Develop a comprehensive plan (April 2004)
 - Validate, define, & extend BEA for Military Equipment
 - IT solution requirements (May 2004)



◆ Real Property, Plant, & Equipment

- Existence and Completeness
- Valuation: need to maintain cost documentation
- Resolve the Leasehold Improvement reporting issue
- Trading Partner information for Real PP&E transferred Intragovernmental

◆ Personal Property -- Properly recognizing internal use software

◆ Military Equipment, Personal Property, and OM&S

- The line of demarcation between Military Equipment, Personal Property, and OM&S will be defined as OUSD(C) & the services proceed with the plan to implement the accounting requirements of SFFAS 23.