DEFENSE COMMISSARY AGENCY

PERFORMANCE AND ACCOUNTABILITY REPORT

Fiscal Year 2005

DECA-AT-A-GLANCE

Established	1991
Headquarters	1300 E Street Ft. Lee, VA 23801 www.commissaries.com www.deca.mil (for authorized parties)
FY 2005 Operations Costs	$1.165 billion
FY 2005 Sales	$5.4 billion
Total Employees	Approximately 18,000
Regional Offices	3 (East, West and Europe)
Commissaries	268 (as of September 30, 2005)
Customers	Approximately 11.8 million

DeCA MISSION• • •

Deliver a Premier Commissary Benefit to the Armed Services Community that:

- Encourages an exciting shopping experience;
- Satisfies customer demand for quality grocery and household products; and
- Delivers exceptional savings while
  - Enhancing quality of life;
  - Fostering recruitment, retention and readiness; and
  - Supporting warfighters' peace of mind, knowing their families have secure and affordable access to American products.

DeCA VALUES• • •

Leadership – **I**ntegrity – **F**lexibility – **E**njoyment

"LIFE": These four words comprise the acronym "LIFE" and are the corporate values DeCA wants employees to represent as the agency moves forward. The values are the engine behind a new vision that highlights DeCA's commitment to the people who deliver and receive the commissary benefit.

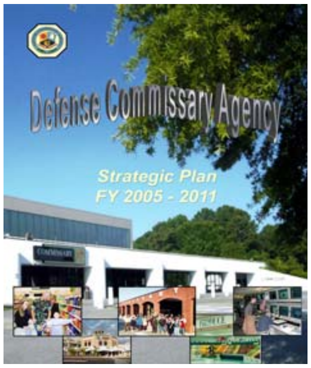
Leadership: We expect passion, courage and excellence!
Integrity: We demand honesty, professionalism and trustworthiness!
Flexibility: We cultivate innovation, empowerment and competence!
Enjoyment: We foster teamwork, recognition and opportunity!

DeCA VISION• • •

Customers, Workforce, Partners → RAVING FANS!

DeCA'S VISION will focus on people – all working together to create "Raving Fans."

DeCA GOALS• • •



Customers: Preserve and Deliver a Premier Quality of Life Benefit

Workforce: Be the Employer of Choice

Partners: Implement Business Process Improvements to Enhance Corporate Performance

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FOREWARD

The Defense Commissary Agency (DeCA), as part of the Department of Defense (DoD), is required to prepare annual financial statements. These financial statements must be prepared in accordance with Office of Management (OMB) directives, which implement the *Chief Financial Officers Act of 1990* (CFO Act). The DoD uses the information in DeCA's annual financial statements to prepare the DoD annual financial statements.

To enhance the presentation of performance, management, and financial information, OMB requires DoD and other agencies to incorporate their annual financial statements into a Performance and Accountability Report (PAR). Although DeCA is not required to prepare a separate PAR, we have prepared this document (closely aligned to the statutory guidance framework) to demonstrate accountability. This PAR provides summary performance information rather than the comprehensive presentation included in the DoD PAR.

PART I

MANAGEMENT'S DISCUSSION AND ANALYSIS

CHIEF EXECUTIVE OFFICER'S MESSAGE

I am pleased to present the annual report of the Defense Commissary Agency's (DeCA) financial and programmatic results for fiscal year 2005. Operating a commissary system with a global mission, the Agency is committed to providing premier quality of life relevancy to its patrons while maximizing the efficiencies and effectiveness of its business processes. During this past year, we have continued our reengineering and restructuring efforts as part of our ongoing commitment to become even more responsive to customer and store-level needs. The new corporate structure will posture DeCA to intensify our focus on stores' needs, reduce corporate costs while optimizing our efficiencies and showcasing the integrity of the commissary benefit—recognized as the premier quality of life benefit of the nearly 12 million authorized patrons we serve.

During fiscal year 2005, DeCA continued the realignment of our business areas and offices as part of our corporate reengineering initiative. Organization processes were realigned to enhance all functions and processes needed to support commissaries on a day-to-day basis and improve functional oversight and policy. We have begun implementation of Lean Six Sigma. Our six Black Belts are each working to improve specific processes. As part of this ongoing effort we are in the process of realigning many of our regional office support functions to the Headquarters.

We eliminated the position of the Agency's Chief Support Officer in July 2005 and established the position of Director, Headquarters Operations. This position will serve as key advisor to the Chief Operating Officer as well as being responsible for the Corporate Operations Group, staff coordination, and logistics support. We also established the position of Chief Financial Executive, replacing the former Comptroller position, which reports directly to the Chief Executive Officer.

The devastating impact of Hurricane Katrina brought out many DeCA heroes, whose Herculean efforts helped re-establish commissary operations at temporary locations in Naval Construction Battalion Center Gulfport and Keesler Air Force Base (AFB), MS, and to reopen the Naval Support Activity (NSA) New Orleans, LA, store. Gulfport sustained major building damage and will have to be restored. The Keesler AFB Commissary was a total loss and will have to be rebuilt. The NSA New Orleans Commissary was only minimally damaged and is now operational again. The Agency also sustained major inventory losses (approximately $3 million) to their resale stocks at eight locations throughout Mississippi, Louisiana, and Florida as a result of the hurricane. An assessment of the total extent of our losses in equipment is still being made.

The Defense Commissary Agency's fiscal year 2005 performance data indicates positive progress in meeting the established performance plan. Through metrics, we directly link resource requirements to desired outcomes supporting the President's Management Agenda and the Department of Defense Balanced Scorecard. Using a business-based approach, we have increased sales while raising customer satisfaction to an all-time high.

We are pleased that for the 4th year in a row, independent auditors have given our financial statements an unqualified opinion. However, the report by the independent auditors on DeCA's internal controls over financial reporting identified areas of nonconformance related to accounting for Property, Plant and Equipment and controls associated with our financial systems. Except for these nonconformances, I certify that DeCA's management control systems, taken as a whole, provide reasonable assurance that the objectives of the Federal Managers' Financial Integrity Act (FMFIA) of 1982 are achieved. In addition, we have evaluated our financial management systems, as required by the Federal Financial Management Improvement Act (FFMIA) of 1996. We found that our systems fall short of the integrated systems requirements. In addition, transactions at the detail level are not compliant with the US Standard General Ledger. The Department of Defense (DoD), with participation by DeCA, is actively working on improving the system-wide architecture for DoD entities that meets the requirements of FMFIA and FFMIA.

As we face both present and future challenges—base closure and realignment, an ever changing marketplace, organizational realignment, and executive branch initiatives—I remain confident in the Agency's unflagging commitment to the enhancement of our business processes to meet those challenges. While continually striving to exceed the expectations of the patrons we serve, we will deliver both a critical economic advantage and a 'taste of home' to our country's Service members deployed around the world. We will remain the premier quality of life benefit to the men and women of the United States Armed Services—relevant, responsive, recognized—a global mission serving a global force—the commissary benefit.

Patrick B. Nixon
Chief Executive Officer

October 31, 2005

OVERVIEW OF DeCA

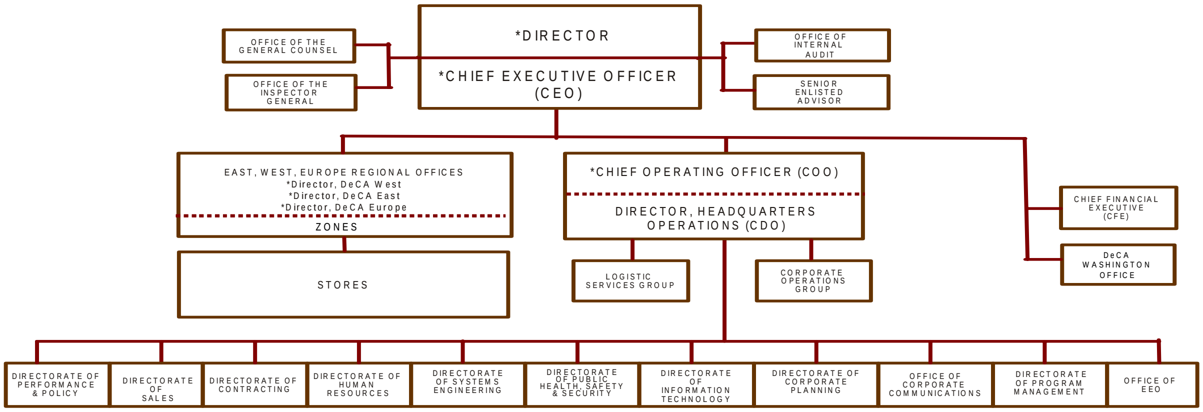
ORGANIZATION:

The Defense Commissary Agency (DeCA) is a component of the Department of Defense (DoD) reporting to the Under Secretary of Defense for Personnel and Readiness. In 1989, the House Armed Services Committee appointed the Jones Commission to analyze the commissary systems (i.e., grocery stores or supermarkets) operated by the four military services. To provide better service for military patrons at a lower cost, the Commission recommended consolidation of the four separate commissary systems. On October 1, 1991, DeCA was established.

DeCA is headquartered at Fort Lee, Virginia. It operates a worldwide system of 268 commissary stores. Three regional offices located in Virginia Beach, Virginia, Sacramento, California and Kaupan Air Station, Germany, provide day-to-day management and support. Our commissaries sell food and related household items to active, reserve and guard members of the Military Departments, their families, retirees, and other authorized patrons. Field Operating Activities perform services for the regional offices and their commissaries, including centralized purchasing of national brand sales items and centralized resale accounting.

Further restructuring of headquarters operations to more sharply focus agency energy and resources on store operations was announced during the 4th quarter of fiscal year (FY) 2005. The Chief Support Officer position was vacant and abolished in the reengineering and reestablished as the Director of Headquarters Operations. The Director of Headquarters Operations serves as a key advisor to the Chief Operating Officer and will have direct oversight of DeCA's Corporate Operations Group, staff coordination, and headquarters logistics support. In addition, DeCA created a Chief Financial Executive position, formerly the DeCA Comptroller, who reports directly to the Chief Executive Officer and Acting Director. The remaining headquarters functional areas and associated process owners will report to the Chief Operations Officer with a renewed emphasis on focusing all available resources for store support.

DEFENSE COMMISSARY AGENCY



* Indicates SES position

August 24, 2005

We continue to emphasize the efficient delivery of the commissary benefit to Armed Services personnel and their families. DeCA continues our business process improvement through the use of Lean Six Sigma to improve performance and resource efficiencies. DeCA has instilled process ownership, greater accountability, efficiency, and effectiveness throughout the commissary system, enabling us to streamline processes at the headquarters, the region and the store levels, and ultimately improving store operations and the commissary benefit.

FY 2005 Highlights

During fiscal year 2005, DeCA's operations included commissaries with annual sales of $5.4 billion and more than 18,000 employees. DeCA operates its commissaries around the world to support the military services. Patrons include approximately 11.8 million active duty military, reservists, retirees, and family members. Congress authorizes DoD to operate its commissaries as a significant non-pay benefit to supplement military income as an integral part of the overall military pay and benefit. DeCA sells its groceries and household supplies to the military community at its cost which, on most grocery items, includes a 1 percent allowance for losses. Patrons also pay a five percent surcharge which funds construction programs and our stores' information management equipment. By selling goods at near cost, DeCA provides the lowest overall prices and the maximum savings benefit to our customers.

The Base Realignment and Closure (BRAC) Commission report sent to Congress in mid-September 2005, included six installations selected for closure that have commissary stores. Commissary stores impacted by the proposed closure decision are Fort Gillem and Fort McPherson, GA; Fort Monmouth, NJ; C.E. Kelly, PA; Naval Air Station Athens, GA; and Naval Air Station Brunswick, ME.

Based on the proposed BRAC increases and decreases at installations impacted by proposed realignments, we have begun positioning ourselves in FY 2005 via the strategic plan to brace for the impact of the BRAC initiatives. Although the exact implications of BRAC 2005 are still unknown, the reality of rightsizing and the limitations on growth and funding make it essential that DeCA posture itself for these proposed actions.

In late August 2005, Hurricane Katrina damaged or destroyed several DeCA facilities. The Key West and Pensacola, FL commissaries sustained roof damage, but incurred no PP&E or inventory losses as a result of the hurricane. The Gulfport, MS commissary suffered interior damage and no real property was written off as a result. The actual losses in equipment at Gulfport are not known and are considered to be immaterial. Gulfport lost their entire resale inventory on hand and as a result the balance was removed from inventory as of September 30, 2005. The Keesler, MS commissary was flooded and, due to significant structural damage, has been declared a total loss. The associated real and personal property has been removed from our financial records. In addition, Kessler lost their entire resale inventory on hand and as a result the balance was removed from inventory as of September 30, 2005. The New Orleans, LA commissary did sustain minor damage, but no inventory or PP&E losses were incurred and the commissary was reopened on September 28, 2005. We have opened temporary stores at Gulfport and Keesler.

SOURCES OF FUNDS:

Within DeCA's working capital fund (WCF) there are two activity groups - Commissary Resale Stocks and Commissary Operations. DoD defines these two activity groups as business areas for fund control purposes. Commissary Resale Stocks finance the purchase of grocery, meat and produce items for resale to authorized patrons. The primary revenue source for this activity group is the sale of inventory to commissary patrons.

Commissary Operations finances the operating costs of resale stores, agency and region headquarters, field operating activities, and support services. The primary revenue source for this activity group is a direct appropriation to the Defense WCF, which in turn transfers the funds to the DeCA WCF. DeCA received approximately $1.2 billion in appropriation transfers during FY 2005. Commissary Operations also receives limited additional revenues from manufacturers' coupon redemption fees, handling fees for tobacco products, and reimbursements for other support.

DeCA's Surcharge Collections Trust Fund is funded, for the most part, from the five percent surcharge applied to each customer sale. This fund, established by law, primarily finances DeCA's store-level information systems equipment and maintenance, as well as its construction programs.

PERFORMANCE GOALS SUMMARY

CORPORATE OBJECTIVES:

DeCA's *Corporate Strategic Plan* is the basis for DeCA's mission, values, vision, goals, objectives and strategies. DeCA's most recent performance plan for FY 2006 - 2011 provides a road map to further improve and enhance the commissary benefit as we continue efforts to increase the number of authorized patrons currently using the benefit. Each objective was designed to enhance DeCA's concept of operations, while keeping service to the customer at the forefront. The commissary benefit clearly is critical to strengthening and preserving the Armed Services quality of life and has an exceptionally positive impact on the recruitment, retention, and readiness of today's military. We are committed to providing our Armed Services military community with a valuable benefit to supplement military income as an integral part of the overall military pay and benefits package. DeCA remains focused on its customers and will offer them greater conveniences and an exciting shopping experience by providing a quality assortment of groceries and household products at a significant savings.

DeCA's STRATEGIC OBJECTIVES, GOALS, AND STRATEGIES

Goals	*Objectives*	*Key Strategies*
Customers *– Preserve and Deliver a Premier Quality of Life Benefit*	Continually improve customer service and sustain customer savings.	▪ Sustain customer savings at 30 percent as measured by DeCA annual pricing study results. ▪ Implement initiatives to attract patrons and improve customer service and satisfaction, as measured by the Commissary Customer Service Survey (CCSS) and the American Customer Satisfaction Index (ACSI).
Workforce *– Be the Employer of Choice*	Foster a corporate culture that creates a satisfying workforce environment and provides opportunities for personal and professional growth.	▪ Reduce employee skill gaps through training and development programs, including DeCA's Corporate Successor Development Program and the Defense Leadership and Management Program ▪ Develop a survey instrument and conduct surveys to establish a baseline, obtain feedback and continually measure progress in terms of employee and manager work place satisfaction. ▪ Link employee performance plans to Agency strategic goals, objectives and performance outcomes. ▪ Enhance the Affirmative Employment Program by identifying barriers to alleviate under-represented categories.
Partners *– Implement Business Process Improvements to Enhance Corporate Performance*	Increase effectiveness and efficiency through disciplined integration of technology, infrastructure and business process improvements.	▪ Reengineer internal business processes through use of Lean Six Sigma procedures to remove non-value added activities and increase support to stores.

Goals	*Objectives*	*Key Strategies*
		▪ Deploy leading edge technologies that integrate business processes, enhance Agency performance and promote interoperability throughout DoD and the military resale systems and with our industry partners. ▪ Continue to implement and maximize use of E-Gov best practices and initiatives to meet Agency needs. ▪ Improve the overall commissary Facility Condition Index (FCI) and capital inventory condition and reduce the backlog by developing and executing approved capital investment fiscal year programs, covering new construction, modernization, maintenance and repair, and store equipment requirements that incorporate state of the art efficiencies. ▪ Control Agency operating costs in accordance with Program Budget targets from the FY 04 baseline without inflation, while considering the full cost of achieving Agency performance goals. ▪ Ensure compliance with DoD's Business Management Modernization Program (BMMP) for conformance on all major information technology investments. ▪ Obtain unqualified opinions through independent audits of financial statements to ensure sound financial performance, including the travel card and purchase card programs. ▪ Study 50 percent of commercially viable candidates in DeCA's inventory by FY 2009, to execute the OMB Circular A-76 competitive sourcing initiative and streamline operations and achieve efficiencies.

FISCAL YEAR 2005 PERFORMANCE GOALS AND RESULTS:

DeCA continues its transformation as a DoD leader in the development and execution of performance and process improvement management practices. We have developed a strong business case for all decisions, using metrics to accurately measure performance. We have embarked on reengineering internal business processes through use of Lean Six Sigma procedures. Lean Six Sigma is a combination of two methodologies – Lean and Six Sigma. Lean is concerned with eliminating waste and improving the flow within a process. Lean eliminates non-value-added steps. Six Sigma focuses on reducing variation and improving process output through the use of specific problem-solving tools. Six Sigma improves quality. By using this methodology, DeCA plans to remove non-value added activities and continue to restructure to become more responsive to store-level needs. Our new corporate structure postures us to better focus on store operations, control corporate costs, and prepare for future challenges.

DeCA's FY 2006 – 2011 Performance Plan provides the performance goals and objectives of the Agency. It articulates the expectations for DeCA's performance during FY 2006 – 2011 in investing in technologies, programs, and product support necessary to achieve and provide the commissary benefit to military personnel and their families. The plan does not alter the basic mission, operations, authority, or reporting channels for the Agency, but complements best business strategies to increase business productivity and increase customer satisfaction by operating effectively and efficiently.

DeCA is currently transitioning to a Norton and Kaplan Balanced Score Card (BSC) methodology and expects implementation in FY 2006. This "business based" approach is well suited for DeCA's mission. The DeCA BSC complements the DoD Risk Management BSC framework and all prior Performance Plan metrics have been included and, where appropriate, includes the President's Management Agenda (PMA) initiatives.

In doing all of the above, we have linked together Planning, Programming, Budgeting and Execution (PPBE) to demonstrate our commitment to both performance improvement and cost reductions. The Agency's strategic plan, corporate objectives, and action plans continue to provide a renewed road map to further improve and enhance the commissary benefit, with a more balanced approach towards achieving our goals and objectives. We have refined our goals and objectives and continually revisit our strategies to better serve our customers, integrate our business processes, and enhance corporate performance. One key performance goal is to earn a clean audit opinion each year from an independent audit firm. As we began our FY 2005 program, we were one of only six of the Department's subordinate financial statement reporting entities that received an unqualified opinion or "clean audit" of our respective FY 2004 financial statements from an independent auditing firm.

PERFORMANCE-AT-A-GLANCE

(Further Explained in the Next Section)

Performance Measure	***FY 2003 Actual***	***FY 2004 Actual***	***FY 2005 Goal***	***FY 2005 Actual***
Customer Savings	32.1%	32.1%	30.0%	32.0%
Commissary Customer Service Survey (CCSS)	4.42	4.47	4.47	4.55
American Customer Satisfaction Index (ACSI)	76	76	76	Available Feb 06
Unit Costs	$0.2172	$0.2146	$0.2186	$0.2171
Facility Condition Index (FCI)	74.50	75.03	79.70	74.94

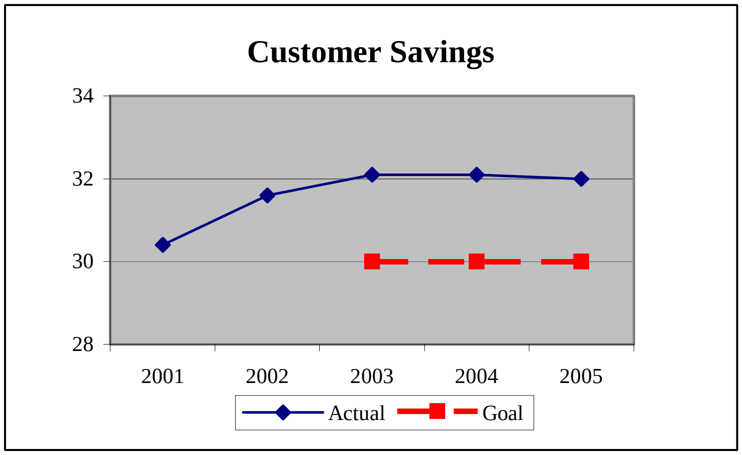
PART II

PERFORMANCE SECTION

PERFORMANCE ANALYSIS

DeCA is on track to exceed its performance goals for FY 2005, except for the Facility Condition Index (FCI). The following charts and discussions illustrate how well our achievements compare to our targets. The charts also depict our performance for the last four years, if data is available. DeCA did not establish some targets until FY 2002 or 2003.

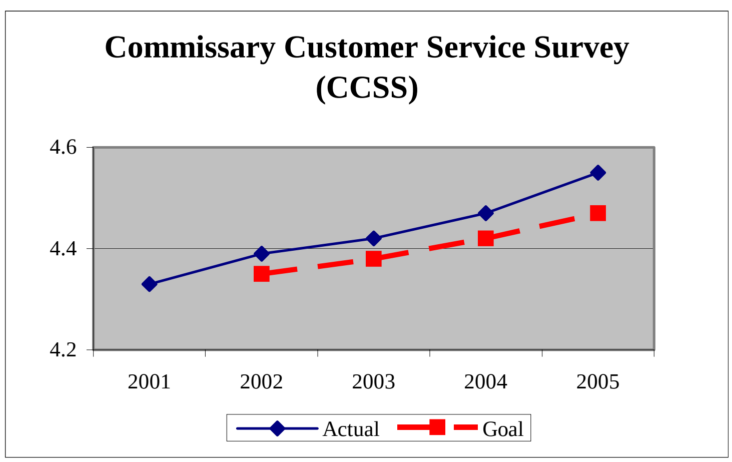
Customer Savings:



Background: The patron savings are calculated using a comprehensive database of actual prices for Universal Product Coded (UPC) items from commercial grocery stores and commissaries to perform the analysis for locations within the 48 contiguous states (over 30,000 items are compiled). All major supermarket chains (e.g., Kroger Co., Winn Dixie, Giant Foods, HEB, etc.) as well as super centers are included in the comparison. Because the database contains only items with a UPC, prices for fresh meat and produce are obtained by physical audit at randomly selected commissaries and nearby commercial grocery stores. This methodology was validated by the Air Force Audit Agency.

Results: DeCA's FY 2005 customer savings of 32.0 percent continues to exceed the goal of 30 percent. Beginning in FY 2005, the market basket sampling survey for commissary savings is conducted in the August/September timeframe of each fiscal year with results tallied and reported by the end of the fiscal year.

Commissary Customer Service Survey (CCSS):

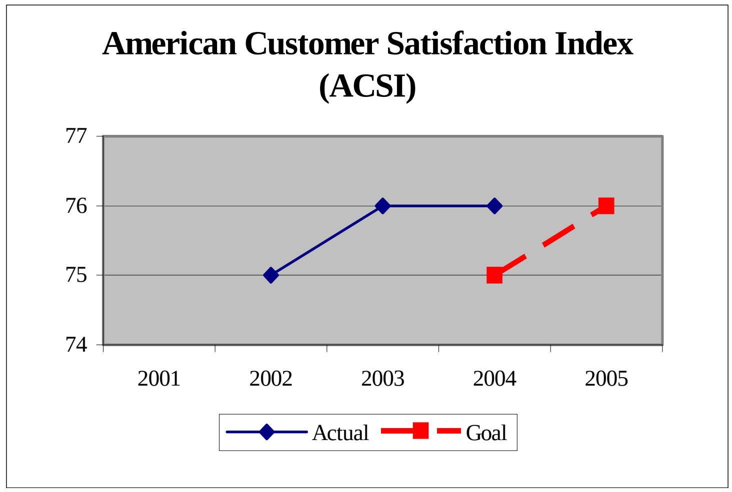


Background: Customer satisfaction is evaluated by surveys based on statistically sound sampling techniques. The CCSS was conducted twice a year prior to FY 2004, but now is being conducted only once per year to allow more time to complete the data collection and analysis. Beginning in FY 2006, surveys will be conducted during the May/June timeframe of each fiscal year with results tallied and reported by the end of that fiscal year. In addition, DeCA incorporated recommendations of a Government Accountability Office (GAO) audit in modifying the method of weighting the surveys. All scores are now weighted to account for differences in commissary size.

Results: The FY 2005 CCSS score of 4.55 exceeded the FY 2005 goal of 4.47 by 2 percent.

American Customer Satisfaction Index (ACSI):

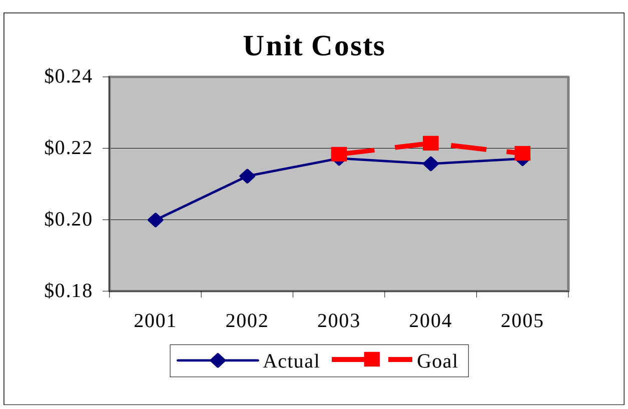
Background: The ACSI is produced annually through a partnership of the University of Michigan Business School, the American Society for Quality, and the consulting firm, Claes Fornell International Group. The ACSI is a uniform, independent measure that is general enough to be comparable across sectors, industries, and organizations of the U.S. economy. The ACSI is measured as a multivariable set of equations and utilizes cause and effect relationships to explain customer loyalty and ties that loyalty to customer satisfaction.



Results: The FY 2004 goal was a score of 75. In the February 2005 report, DeCA received a score of 76 for FY 2004. This score was above the grocery industry average of 73, equal to the score received in FY 2003, and above the score of 75, which DeCA received in FY 2002. The FY 2005 results of the ACSI will not be available until February 2006.

Unit Costs:

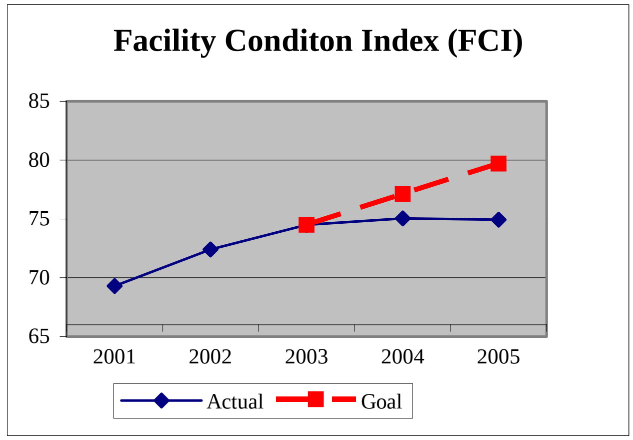
Background: Unit cost is the total of commissary operating costs divided by the total commissary sales revenue. The FY 2005 performance plan sets the unit cost metric goal at $0.2186, based on an operating costs goal of $1,169.4 million and a sales goal of $5,349.4 million.



Results: Actual unit cost was $0.2171 as of September 30, 2005.

Facility Condition Index (FCI):

Background: The FCI is a numerical expression of the physical state of a commissary store. The FCI is a weighted measure of a commissary's condition, refrigeration system, and energy usage and efficiency. The FCI reflects the overall condition of commissary plant and facilities. The goal for FY 2005 is a score of 79.7. The FCI is used as a leading indicator in assessing the effectiveness of the investment of surcharge funding in the physical facilities program.



Results: FY 2004 FCI results were reported in February 2005, with a score of 75.03. Beginning in FY 2005, FCI will be conducted during the June/July timeframe of each fiscal year with results tallied and reported by the end of the fiscal year. The FY 2005 year-end results have been tallied with a resulting score of 74.94, which is 94.03% of the goal. The actual results fell short of the goal due to aged refrigeration systems, first-time assessments for new and upgraded stores, and additional energy use. As a result, DeCA has reviewed the original goals and has developed recommended adjustments. Upon review and approval, the FCI goals will be adjusted accordingly.

ACCOMPLISHMENTS

Since FY 2001, the Defense Commissary Agency (DeCA) has implemented several initiatives that support the President's Management Agenda (PMA) and have resulted in improved levels of service to our customers, corporate succession planning, reduction in skill gaps, and more effective use of our resources to honor DeCA's commitment to prudent stewardship of taxpayer funds.

To improve performance and reduce cost through competition, DeCA decided to develop a "whole store" competition plan. To determine the viability of the "whole store" model, DeCA created a most efficient organization (MEO) and chose a store as a prototype to test the model. The new prototype store features a multiskilled workforce, trained in all areas of the store operations. DeCA anticipates simplified hiring, greater productivity, more efficient work scheduling, increased customer service and reduced labor costs. On January 23, 2005, the Smokey Point Commissary, WA became DeCA's first official prototype store. After approximately six months of testing and evaluation against established baselines, a second prototype store, Grand Forks, ND, was established.

DeCA's Succession Planning Policy is an integral component of the Agency Corporate Development Program. The Intern, Corporate Successor Development Program (CSDP), upward mobility and other development programs are in place to ensure continual development of future leaders in DeCA. DeCA's established a CSDP Council which is staffed with senior officials and a CSDP training catalogue is under development. This catalogue is another tool for maximizing employee self development ensuring that every employee, no matter where their organizational location, has access to a positive training experience via the classroom, video tape, conference, web-based programs, or seminars/workshops.

The Commissary Career Program (CCP) and the CSDP ensure a steady pipeline of highly qualified and trained individuals to fill anticipated vacancies in key mission critical and senior leadership positions. The primary occupation in DeCA is commissary management. There are 1,152 employees registered in the CCP. During the 3rd quarter, FY 2005, there were 42 CCP referrals and selections under the program. Through CSDP, the Agency makes a concerted effort to identify competencies required by commissary management specialists to become future leaders of the Agency and develop these employees to become proficient in identified competencies. DeCA plans to expand CSDP to lower graded commissary management employees. This will support our effort to ensure a cadre of highly qualified and well trained employees exist at every level of commissary management.

The primary focus of DeCA's CSDP is succession planning to ensure the availability of sufficient high potential individuals to fill key senior leadership positions likely to be vacated over the next five years. During FY 2005, twenty-five selections were made. In addition to the CSDP, DeCA also utilizes the Defense Leadership and Management Program (DLAMP) to satisfy some training needs for executives. One employee graduated from DLAMP this past December and four more remain as active participants. Three DeCA executives participated in the Federal Executive Institute (FEI) "Leadership for a Democratic Society" program during FY 2005. Two employees graduated from the Executive Leadership Development Program during FY 2005.

As compared to the 2000 Census data, all groups except Caucasian females and Hispanic males are at overall parity within the Agency. During the last reporting period, the Agency showed an increase in the workforce population of 310. The agency showed an increase of African Americans, Hispanics, Asians and American Indians, although the workforce representation percentages remained virtually the same. DeCA's primary goal is to increase representation of minorities and females at the GS-13 level and above. Additionally, the agency has set goals to increase the representation, as needed, of females, Hispanics, African Americans, Asians and people with targeted disabilities.

The PMA requires that all operational mission essential and mission support IT systems be certified and accredited by the Defense Information Technology Security Certification and Accreditation Process (DITSCAP). There are a total of seven mission essential systems for DeCA: Standard Automated Voucher Examination System (SAVES), Warehouse Management System (WMS), Commissary Online Product Pricing System (COPPS), Electronic Data Interchange (EDI), Point of Sale (POS), DeCA Interactive Business System (DIBS), and Computer Assisted Ordering (CAO). During FY 2004, five of the seven mission essential systems achieved Approval to Operate (ATO) status, while the remaining two achieved Interim Approval to Operate (IATO) status during FY 2005. In addition, there are a total of five mission support systems: Corporate Human Resources Information System (CHRIS), Accounting and Inventory Management System (AIMS), Enterprise Data Warehouse (EDW), Automated Vendor

Credit Memorandum (AVCM) and Central Meat Processing Plant (CMMP). Two of these systems have achieved ATO status, two are in the DITSCAP process, and one does not require certification and approval at this time as it is in development phase. All network and enterprise platforms have received ATO status.

NEAR AND LONG-TERM PLANS

DeCA's Enterprise Business System (DEBS) is a new system in development that will retire multiple legacy systems that currently support the cataloging, ordering, receiving, inventory accountability, and promotions business processes. The systems identified for replacement by FY 2011 include the DeCA Interactive Business System (DIBS), Automated Vendor Credit Memorandum (AVCM), Computer Assisted Ordering (CAO), Sales Order System (SOS), Commissary Online Product Pricing System (COPPS), Web Pricing, Warehouse Management System (WMS), Central Meat Processing Plant (CMPP), Store Ordered/Vendor Shipped (STO/VES) and Meat/Produce. DEBS received approval to obligate FY 2005 funding for Pre-Milestone A, and Fiscal Year 2006 funds for Milestone A - concept refinement work and startup of an acquisition program. DEBS Functional Integrated Process Team (IPT) completed a Business Model and is using the model as the premise for identifying requirements. The Business Model requirements and disciplines identify system and business redundancies that exist today. Using this methodology, the DEBS IPT is streamlining the functions and processes to reduce the DEBS overall cost.

Data Management Strategy. DeCA completed the implementation of the initial release of the commercial off-the-shelf (COTS) Retail Logical Data Model (RLDM). RLDM defines the relationship of the data stored in the Electronic Data Warehouse. Development of FY 2006 milestones is being worked. FY 2006 milestones will exploit the additional capabilities available in the RLDM, and include data centralization, data standards, and data sharing.

Organization and Process Reengineering. DeCA expects to complete reengineering implementation in FY 2006 - 2007 by consolidating some corporate and store support functions such as procurement, comptroller, operations, and human resources at DeCA headquarters, eliminating layering. This above-store level reengineering process is ongoing and consistent with BRAC guidance. Effective May 1, 2005, 32 stores were shifted from DeCA East to DeCA West to balance the Continental United States (CONUS) span of control. These actions are consistent with observations by the GAO in its report 01-473, April 2001, "Defense Infrastructure – Commissary Savings Should Produce Savings but Opportunities May Exist for More," to consolidate the three U.S. regional offices into two and balance the number of stores in each.

Competitive Sourcing. The Agency's overall goal is to compete 6,392 full-time equivalents (FTEs) or 50 percent of the 12,784 FTEs in the Federal Activities Inventory Reform Act (FAIR) inventory of FY 2000. To date, DeCA has completed competitions on 3,572 FTEs or 56 percent of the Agency's overall goal. In continuing planned competitive sourcing efforts through FY 2008, DeCA is currently performing its preliminary planning, which is required to be completed prior to the announcement of a competition. There is no change to the FTE milestone table data.

Commissary Advanced Resale Transaction System (CARTS). CARTS is a major acquisition program to replace the commissary's current point of sale system. DeCA received Milestone A approval (Concept Refinement Phase) from the Acting Director, Networks and Information Integration (NII) in February 2005 to enter the Technology Development Phase and is on schedule to pass Milestone B (Procurement Strategy, Systems Requirements, Economic Analysis, and Test and Evaluation Master Plan) in FY 2006. Milestone B approval allows DeCA to select the vendor and test the system. By the end of the first quarter FY 2006, DeCA will award the CARTS contract based on best value to the government through a competitive solicitation. The CARTS team will work with the new CARTS vendor for the remainder of FY 2006 to complete various stages of testing to prepare the system for deployment. Those tests involve an Operational Capabilities Demonstration of the CARTS system to ensure it complies with contractual requirements and integration testing to ensure the system operates properly within DeCA's commissary environment. A Milestone C decision, System Development and Demonstration Phase, will be granted upon successful testing at the end of FY 2006. That milestone decision will allow DeCA to begin Operational Testing and ultimately fully deploy the system in FY 2007.

Radio Frequency Identification (RFID). The OSD Supply Chain Integration (SCI) Office held a meeting during the 3rd Quarter, FY 2005 with the resale components, which included DeCA, the Army and Air Force Exchange Service (AAFES), and the Navy Exchange Service Command (NEXCOM) to discuss future RFID implementation plans. DeCA advised SCI that the Agency is revising its RFID Implementation Plan based on the current technology issues associated with passive RFID, slow grocery industry response, and major ongoing system initiatives in DeCA. DeCA's revised plan recommends passive RFID deployment begin in 2010 with the Central Distribution Centers and finish in 2014 with deployment to the commissaries.

In summary, DeCA's past performance and FY 2005 performance indicates positive progress and articulates the expectations for DeCA's investment in human capital, technologies, programs, and product support necessary to achieve and provide the commissary benefit to military personnel and their families.

CONTROLS AND STATEMENT OF FINANCIAL ASSURANCE

DeCA accepts the responsibility of reporting performance and financial data accurately and reliably with the same vigor as we accept and conduct business and manage commissary operations. All performance data for this report is gathered and reported through a system of rigorous controls and quality checks. Representatives from each directorate or process gather year-end performance data from their respective program and project officers. The process owners and/or directors for each area or office review and validate this data. System / staff accountants and analysts in the Office of the Chief Financial Executive also review this data before it is archived with all pertinent source information. In addition, DeCA uses various management information systems regularly to track and report on performance, and financial data. Fiscal year 2005 marked the second year that DeCA produced financial reports within accelerated timeframes.

While the financial audit is not a new process, we experienced significant challenges to ensure data accuracy and its validation. Critical transactional data was identified, documented, tested, and converted to comply with proposed recommendations. Therefore, DeCA dedicated resources throughout the Agency to analyze and reconcile data elements related to financial reporting.

IMPROPER PAYMENTS

In compliance with the Improper Payments Information Act of 2002 and specific guidance from the Office of Management and Budget, DeCA used a systematic process for reviewing all programs that are susceptible to significant improper payments. In FY 2004, DeCA resource management locations were tasked to sample payments to determine the rate, volume, and amount of payments that were made improperly. DeCA's results were better than the Office of Management and Budget error rate threshold and therefore DeCA was considered not at risk for significant improper payments. Our low rate of improper payments is due in large part to strong internal controls. DeCA had pursued a recovery audit contract to assist in identifying and recouping erroneous payments, but because of DeCA's compliance status, it was not necessary to continue the contract.

FEDERAL MANAGERS FINANCIAL INTEGRITY ACT (FMFIA) STATEMENT OF ASSURANCE

In FY 2005, DeCA reported an unqualified assurance statement. In determining the type of assurance, the director considered information from various sources, including management reviews, Inspector General and Government Accountability Office reports, audits of financial statements, reviews of financial and computer systems, and other information provided by committees of jurisdiction. Internal management control reports and assessments discussed those issues considered to be material at the Agency level. However, it was just one piece of the DeCA's multi-faceted reporting strategy. Other elements of the strategy included our internal performance and results report, through which we presented annual measurements of DeCA's performance indicators and, our annual financial statement and audit report, which presented findings from an independent auditor.

In FY 2004, in a continuing effort to improve the Department's management controls, the DoD Comptroller continued its implementation of a senior level review matrix, or scorecard, to address management accountability and related issues within the broader context for the services and its components. This scoring matrix graded assurance statements in five categories: timeliness, format, program execution, training, and material weakness reporting. It also helped DoD to communicate the importance of management controls and evaluated the effectiveness of its execution process by benchmarking components and recognizing top achievers.

DeCA received congratulatory comments and commendations for tying for second place in DoD with two other commands and was rated as most improved for its management control program.

PART III

FINANCIAL SECTION

CHIEF FINANCIAL EXECUTIVE'S MESSAGE

Fiscal Year (FY) 2005 was a year of continued improvements and refinements in overall DeCA management. Accomplishments in the area of financial processes and accountability were especially noteworthy as the Defense Commissary Agency (DeCA) led the Department of Defense (DoD) in Real Property reconciliation (with the various Services). The real property reconciliation was required by DoD to determine the preponderant users of buildings DeCA utilizes, but does not own, in order to record them on the books of the primary user. In addition, DeCA earned an independent "unqualified" audit opinion at the end of FY 2005. This significant accomplishment made DeCA one of the select group of DoD agencies who earned four consecutive annual unqualified audit opinions from an independent audit firm.

The DeCA audit committee – with members from OSD (Comptroller), DoD (Inspector General), DFAS, our independent audit firm (KPMG) and multiple DeCA offices - met regularly to discuss issues, develop policies and implement procedures to enhance accountability and financial management. The committee maintained oversight of the audit progress, improvements in real property reconciliation, and all property, plant and equipment activity. With 268 commissaries worldwide, these efforts were complex and demanding on all parties. Nevertheless, real progress is evident as DeCA continues to conduct wall-to-wall inventories to ensure complete and accurate reports of assets.

Internal control efforts were also a management focus and DeCA's efforts were recognized by DoD for FY 2004 as having the most improved Internal Control Program and for also tying for 2nd place for the overall report. For FY 2006, DeCA is beginning the intensive management efforts required to meet the new OMB Circular A-123, Appendix A requirements. This work will culminate in a separate management Statement of Assurance of effective internal controls over financial reporting.

The latest DoD Base Realignment and Closure (BRAC) initiative is anticipated to impact DeCA commissaries at multiple locations as early as March 2006. While several installation closures are anticipated, force realignment and consolidation at other installations will require additional shifting of DeCA facilities and personnel. The full impact of the ongoing BRAC initiative will not be clear until the legislation is passed by the Congress and signed by the President in November 2005.

Despite significant challenges, DeCA excelled in most aspects of performance measurement. Sales were higher than forecast while operating costs were contained – resulting in a low unit cost. Customer satisfaction scores – measured by the American Customer Service Index (ASCI) and Commissary Customer Service Survey (CCSS) – were high. In keeping with the DoD focus, DeCA is also transitioning to a Balanced Scorecard process in FY 2006 which will incorporate and/or compliment the efforts underway in the President's Management Agenda. Patron saving continued to exceed the goal of 30 percent by achieving an average of 32 percent.

Thus, the commissary benefit remains a major quality of life benefit for Service members around the world.

In summary, FY 2005 brought management challenges on multiple fronts to DeCA, but teamwork, attention to detail, and open dialogue with all stakeholders led to improvements and high value to DoD and patrons. We look forward to continued growth and even more notable accomplishments in FY 2006.

Pamela F. Conklin
Chief Financial Executive

October 31, 2005

FINANCIAL STATEMENT SUMMARY

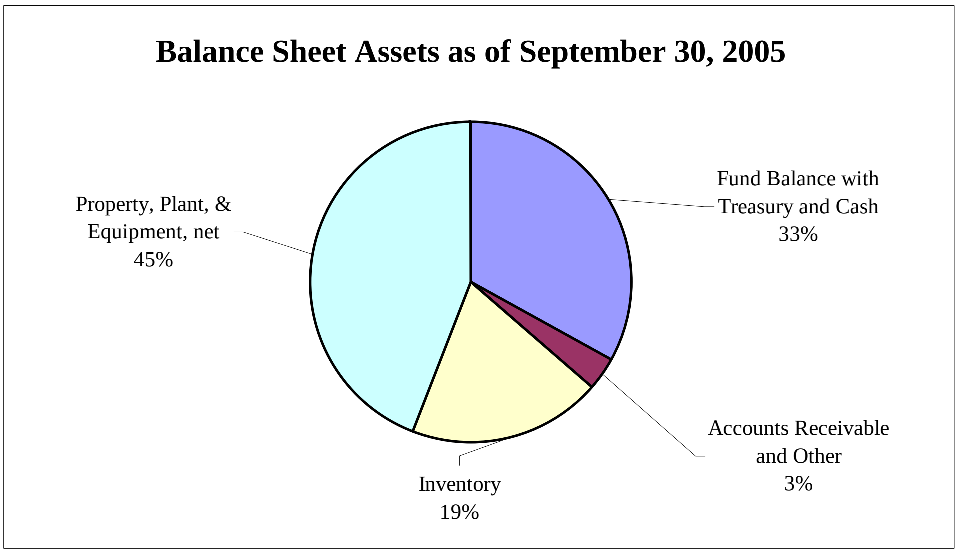
DeCA's financial statements have been prepared to report the financial position and results of operations for the entity, pursuant to the requirements of Title 31, U.S.C. 35125 (b). These statements have been prepared from DeCA's books and records in accordance with the formats prescribed by the Office of Management and Budget (OMB). These statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records. The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity. As such, some liabilities cannot be liquidated without legislation that provides resources to do so.

DeCA's Consolidated Balance Sheets, Statements of Net Cost, Changes in Net Position, Financing, and Combined Statements of Budgetary Resources are presented in a two-year comparative format, as required by OMB Circular A-136, *Form and Content of the Performance and Accountability Report (PAR) Financial Statements*, dated August 23, 2005. The following section provides a brief description of (a) the nature of each required financial statement and its relevance to DeCA, (b) significant fluctuations from FY 2004 to FY 2005, and (c) certain significant balances, where necessary, to help clarify their link to DeCA's operations.

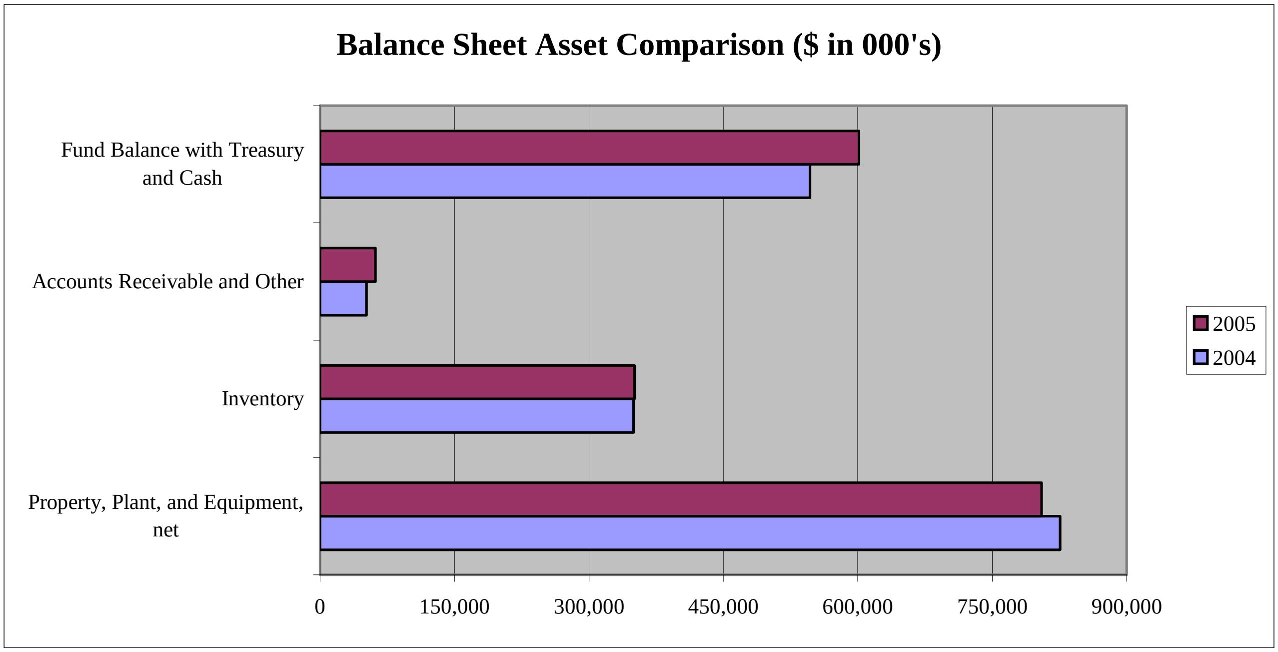
Balance Sheet:

The Balance Sheet presents the amounts available for use by DeCA (assets) against the amounts owed (liabilities) and amounts that comprise the difference (net position).

Assets – As of the September 30, 2005, DeCA's assets were $1,819 million. The assets of DeCA are the resources available to pay liabilities or satisfy future service needs. DeCA's major categories of assets, as a percentage of total assets are as follows:



The following chart presents comparative data of major asset balances as of September 30, 2004 and September 30, 2005. A discussion of significant fluctuations follows.



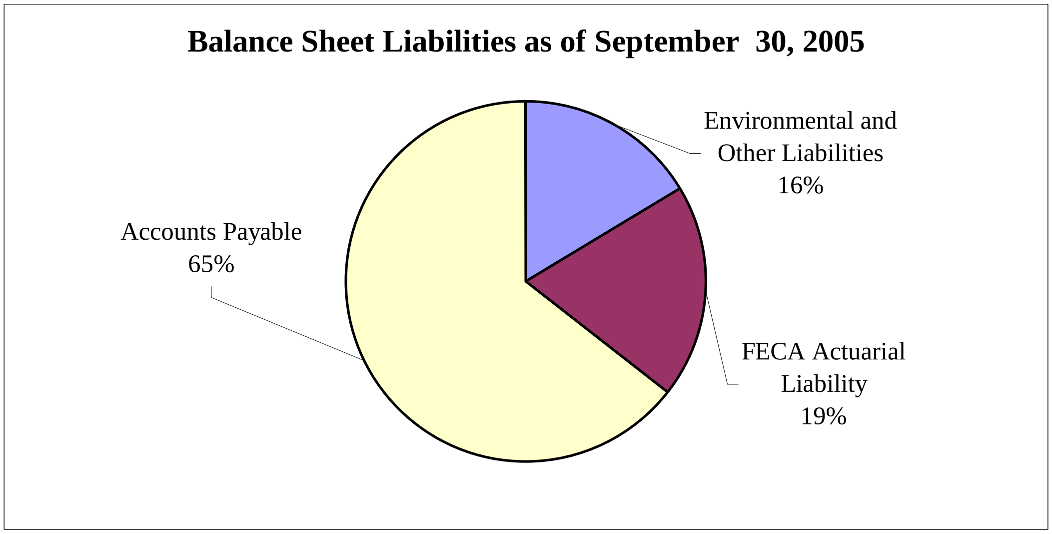
Fund balance with Treasury (FBWT) and Cash is primarily funding available through U.S. Department of the Treasury accounts from which DeCA is authorized to make expenditures to pay liabilities. It also includes monies available at commissaries, or those deposits that have not yet been deposited to the U.S. Department of the Treasury. As of September 30, 2005, DeCA has an overall $601.4 million or 33 percent of its assets in fund balance with Treasury and cash. This is an increase of $55 million, or 10 percent, over the prior year balance, due to increases in sales, surcharge collections, and appropriations transfers.

Accounts Receivable and Other primarily represents amounts due from governmental and public customers of DeCA. Accounts receivable and other increased by approximately $10 million, or 19 percent. This increase was primarily caused by increased sales during the month of September 2005, whereby the associated collections did not occur until October 2005.

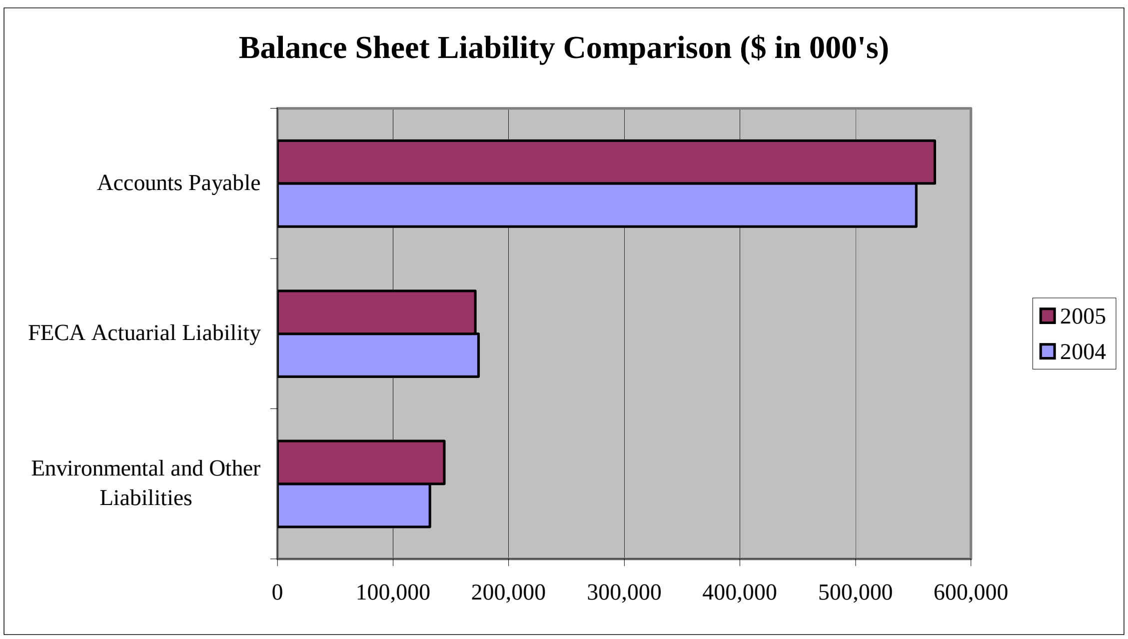
Inventory represents 19 percent of DeCA's current year assets, and comprises grocery products held for resale to patrons at DeCA facilities. Inventory increased by $1 million, or less than 1 percent, over prior year.

General Property, Plant and Equipment (PP&E), net represents 45 percent of DeCA's current year assets, and is primarily comprised of capitalized real and personal property held to fulfill DeCA's mission of selling groceries to its patrons. PP&E decreased by $21 million, or 3 percent from FY 2004. This decrease includes adjustments related to the retirement of PP&E as a result of Hurricane Katrina, as well as normal depreciation on existing property and equipment.

Liabilities - On September 30, 2005, DeCA reported liabilities of $884 million. Liabilities are probable and measurable future outflows of resources arising from past transactions or events. The chart below depicts DeCA's major categories of liabilities as a percentage of total liabilities.



The following chart presents comparative data of major liability balances as of September 30, 2004 and September 30, 2005. A discussion of significant fluctuations follows.



Accounts Payable consists of DeCA's current liability for goods and services delivered or received, but not yet paid, prior to year-end. DeCA's accounts payable increased by $15 million, or 3 percent. The increase was primarily due to higher year-end purchases of inventory.

Federal Employees Compensation Act (FECA) Actuarial Liability comprises 19 percent of DeCA's current year liabilities, and consists of DeCA's expected liability for death, disability, and medical costs for approved workers compensation cases, plus a component for incurred but not reported claims. The Department of Labor (DoL) calculates the liability for the DoD, and DoD attributes a proportionate amount to DeCA based upon actual workers' compensation payments to DeCA employees over the preceding four years. The actuarial liability decreased by $3 million in FY 2005, or 2 percent because of the decreased amount allocated to DeCA by the DoD.

Environmental and Other Liabilities are potential costs to clean up items such as asbestos, lead paint and other hazardous materials from our commissaries. It also includes liabilities for accrued payroll and benefits, accrued unfunded leave, and foreign national separation pay. These liabilities increased $13 million or 10 percent from FY 2004. The increase is primarily the result of a change in the methodology for estimating environmental liabilities, which resulted in an increase of $23 million to our environmental liabilities. This increase was offset by a $10 million decrease in other liabilities.

Statement of Net Cost:

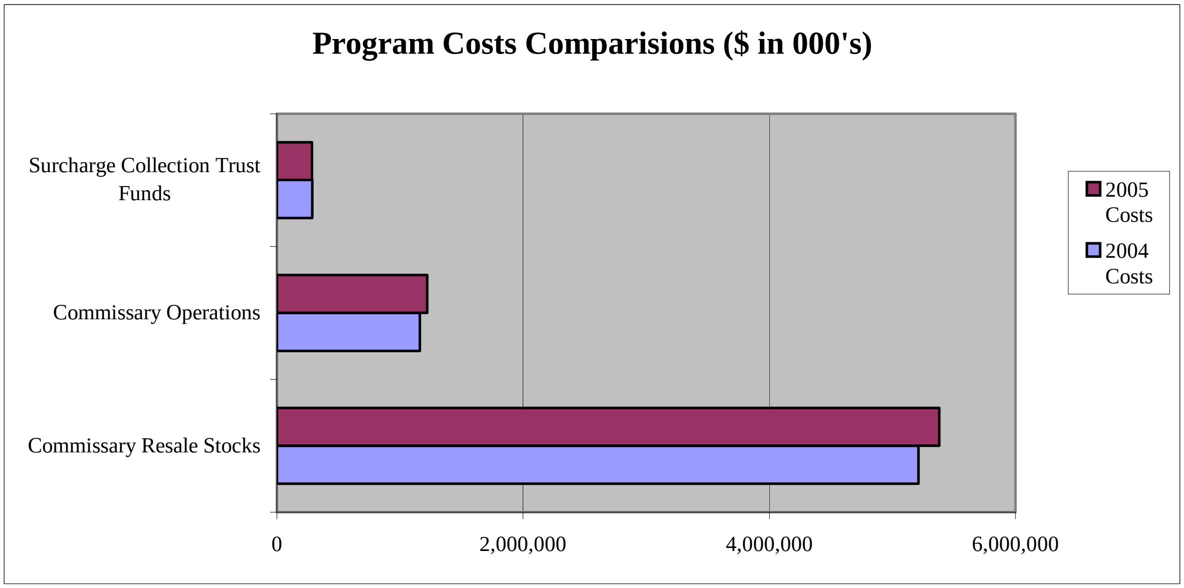
The Statement of Net Cost presents the annual cost of operating DeCA programs. The gross costs for DeCA less the earned revenue from grocery sales and other revenue sources are used to derive DeCA's net cost of operations. DeCA's gross costs are primarily accounted for in the three major activity groups of DeCA:

- *Surcharge Collections Trust Fund* includes the costs to construct and remodel commissary facilities;

- *Commissary Operations* includes the associated payroll and operational costs necessary to operate the commissary system; and

- *Commissary Resale Stocks* includes the costs to purchase grocery inventory for resale.

The chart on the following page compares the gross costs between FY 2004 and FY 2005 in these three major DeCA activity groups:



Total revenues and costs each increased approximately 3 percent in FY 2005 primarily as a result of increased sales and increased purchases to support sales.

Statement of Changes in Net Position:

The Statement of Changes in Net Position represents those accounting transactions that caused the net position of the balance sheet to change from the beginning to the end of the reporting period. Various financing sources increase net position, including appropriations transfers and imputed financing from costs absorbed by others. DeCA's net cost of operations serves to reduce net position.

DeCA's net position increased by $19 million, or 2 percent - from $915 million in FY 2004 to $934 million in FY 2005. The change in net position resulted from a $32 million increase in FY 2005 unexpended appropriations offset by a $13 million decrease in the cumulative results of operations.

Statement of Budgetary Resources:

This statement provides information on the budgetary resources available to DeCA for fiscal year 2004 and 2005, and the status of those budgetary resources at year-end. The outlays reported on this statement reflect the actual cash disbursed for the year by Treasury for DeCA's obligations. The budgetary resources increased by $242 million, or 4 percent from FY 2004 to FY 2005, which is primarily attributed to an increase in appropriation transfers and spending authority from offsetting collections.

Statement of Financing:

This statement reconciles the resources available to DeCA to finance operations, and the net cost of operating the commissary system. *Change in budgetary resources obligated for goods, services, and benefits ordered but not yet provided* includes the change in undelivered orders and unfilled customer orders. *Resources that finance the acquisition of assets* are additions and reductions to capital and other asset balances during the fiscal year. *Components requiring or generating resources in future periods* disclose the net increase in liabilities that are not covered by current budgetary resources.

LIMITATIONS OF THE FINANCIAL STATEMENTS

DeCA prepared its financial statements to report its financial position and results of operations, pursuant to the requirements established by the Department of Defense (DoD) to comply with the *Chief Financial Officers Act of 1990* and the *Government Management Reform Act of 1994.*

While DeCA's statements have been prepared from its books and records in accordance with the formats prescribed by the Office of Management and Budget (OMB), the statements are, in addition to the financial reports, used to monitor and control budgetary resources, which are prepared from the same books and records.

These statements should be read with the understanding that they are for a component of the U.S. Government, a sovereign entity. The U. S. Congress cannot liquidate liabilities not covered by budgetary resources without the enactment of an appropriation, and the Federal Government, other than for contracts, can abrogate payment of all liabilities.

DEFENSE COMMISSARY AGENCY
CONSOLIDATED BALANCE SHEETS
AS OF SEPTEMBER 30
(in thousands)

	2005	2004
Assets		
Intragovernmental:		
Fund balance with Treasury (Note 2)	$ 502,163	$ 450,368
Accounts receivable and other	539	252
Total intragovernmental assets	502,702	450,620
Cash	99,198	96,318
Accounts receivable and other	61,079	51,387
Inventory	350,948	349,794
General property, plant, and equipment, net (Note 3)	804,914	825,787
Total assets	$ 1,818,841	$ 1,773,906
Liabilities (Note 4)		
Intragovernmental:		
Accounts payable	$ 121,443	$ 150,753
Other	39,898	39,976
Total intragovernmental liabilities	161,341	190,729
Accounts payable	447,293	401,990
Federal Employees Compensation Act actuarial liability	171,207	174,076
Environmental liabilities	31,866	9,015
Other	72,665	82,834
Total liabilities	884,372	858,644
Commitment and contingencies (Note 9)		
Net position (Note 5)		
Unexpended appropriations	50,384	17,816
Cumulative results of operations	884,085	897,446
Total net position	934,469	915,262
Total liabilities and net position	$ 1,818,841	$ 1,773,906

The accompanying notes are an integral part of the financial statements.

DEFENSE COMMISSARY AGENCY
CONSOLIDATED STATEMENTS OF NET COST
FOR THE YEARS ENDED SEPTEMBER 30
(in thousands)

	2005	2004
Program costs		
With the public	$ 6,144,729	$ 5,874,637
Intragovernmental (Note 6)	744,254	787,470
Total	6,888,983	6,662,107
Earned revenue		
From the public	(5,673,785)	(5,521,946)
Intragovernmental	(9,766)	(3,932)
Total	(5,683,551)	(5,525,878)
Net cost of operations	$ 1,205,432	$ 1,136,229

The accompanying notes are an integral part of the financial statements.

DEFENSE COMMISSARY AGENCY
CONSOLIDATED STATEMENTS OF CHANGES IN NET POSITION
FOR THE YEARS ENDED SEPTEMBER 30
(in thousands)

	2005		2004	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
Beginning balances	$ 897,446	$ 17,816	$ 860,195	$ (135,706)
Budgetary financing sources				
Appropriation transfer	-	1,174,609	-	1,089,482
Appropriations transfers used	1,140,999	(1,140,999)	1,098,834	(1,098,834)
Non-exchange revenue	21,359	-	21,190	-
Transfers in/out (Note 8)	729	(929)	163,100	-
Equity transfer (Note 8)	-	-	(163,100)	163,100
Other	(1,898)	(113)	16,582	-
Other financing sources				
Imputed financing (Note 7)	36,028	-	36,648	-
Other	(5,146)	-	226	(226)
Total financing sources	1,192,071	32,568	1,173,480	153,522
Net cost of operations	1,205,432	-	1,136,229	-
Net change	(13,361)	32,568	37,251	153,522
Ending balances	$ 884,085	$ 50,384	$ 897,446	$ 17,816

The accompanying notes are an integral part of the financial statements.

DEFENSE COMMISSARY AGENCY
COMBINED STATEMENTS OF BUDGETARY RESOURCES
FOR THE YEARS ENDED SEPTEMBER 30
(in thousands)

	2005	2004
Budgetary resources (Note 8)		
Budget authority	$ 1,189,778	$ 1,098,948
Unobligated balance brought forward	(27,097)	(193,586)
Net transfers and adjustments	701	163,173
Spending authority from offsetting collections	5,681,421	5,530,387
Recoveries of prior year obligations	12,521	21,353
Permanently not available	(4,604)	(10,167)
Total budgetary resources	$ 6,852,720	$ 6,610,108
Status of budgetary resources		
Obligations incurred		
Direct	$ 1,142,469	$ 1,106,751
Reimbursable	5,698,779	5,530,454
Total obligations incurred	6,841,248	6,637,205
Unobligated balance	11,472	(27,097)
Total status of budgetary resources	$ 6,852,720	$ 6,610,108
Relationship of obligations to outlays		
Obligated balance, net - beginning of period	$ 749,542	$ 746,426
Total obligations incurred	6,841,248	6,637,205
Less: spending authority from offsetting collections and recoveries of prior year obligations	(5,693,942)	(5,551,740)
Obligated balance, net - end of period	(774,090)	(749,542)
Total outlays	$ 1,122,758	$ 1,082,349
Outlays		
Disbursements	$ 6,804,907	$ 6,639,668
Collections	(5,682,149)	(5,557,319)
Total outlays	$ 1,122,758	$ 1,082,349

The accompanying notes are an integral part of the financial statements.

DEFENSE COMMISSARY AGENCY
CONSOLIDATED STATEMENTS OF FINANCING
FOR THE YEARS ENDED SEPTEMBER 30
(in thousands)

	2005	2004
Resources used to finance activities		
Budgetary resources obligated:		
Obligations incurred	$ 6,841,248	$ 6,637,205
Less: Spending authority from offsetting collections and recoveries	(5,693,942)	(5,551,740)
Obligations, net of offsetting collections and recoveries	1,147,306	1,085,465
Other resources:		
Imputed financing from costs absorbed by others (Note 7)	36,028	36,648
Other	(5,146)	-
Net other resources used to finance activities	30,882	36,648
Total resources used to finance activities	1,178,188	1,122,113
Resources used to finance the net costs of operations		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:		
Undelivered orders	(21,686)	3,483
Unfilled customer orders	(587)	(91)
Resources that fund expenses recognized in prior periods	(3,221)	(25,881)
Resources that finance the acquisition of assets and other	(5,158,296)	(5,009,336)
Total resources used to finance items not part of the net cost of operations	(5,183,790)	(5,031,825)
Total resources used to finance the net cost of operations	(4,005,602)	(3,909,712)
Components of the net cost of operations that will not require or generate resources in the current period		
Components requiring or generating resources in future periods -		
Increase in exchange revenue receivable from the public and other	8,158	6,510
Components not requiring or generating resources in future periods:		
Cost of goods sold	5,091,390	4,904,126
Depreciation and amortization	91,685	116,313
Revaluation of assets/liabilities	(1,765)	(2,458)
Non-exchange revenue and other	21,566	21,450
Total components of net cost of operations that will not require or generate resources in the current period	5,211,034	5,045,941
Net cost of operations	$ 1,205,432	$ 1,136,229

The accompanying notes are an integral part of the financial statements.

DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. <u>Description of Reporting Entity</u>

The Defense Commissary Agency (DeCA) provides grocery, meat, and produce items to members of the U. S. Armed Forces, their dependents, retirees, and other authorized patrons, including other governmental entities. DeCA is a Department of Defense (DoD) agency under the control of the Under Secretary of Defense for Personnel and Readiness. DeCA was created in 1991 after the House Armed Services Committee-appointed Jones Commission recommended that a single agency be responsible for operating the military commissary system to increase effectiveness at a lower cost.

DeCA, with its headquarters located at Fort Lee near Petersburg, Virginia, has three regional offices located at Kaiserslautern, Germany; Virginia Beach, Virginia; and Sacramento, California. DeCA operations are financed primarily by a working capital fund (WCF) and surcharge collections.

DeCA's WCF is considered part of the DoD's WCF, which includes the financial activity of several Defense Agencies. Within DeCA's WCF, there are two activity groups, Commissary Resale Stocks and Commissary Operations. DoD defines these two activity groups as business areas for fund control purposes. Commissary Resale Stocks finances the purchase of grocery, meat and produce items for resale to authorized patrons. The primary revenue source for this activity group is the sale of inventory to commissary patrons. Commissary Operations finance the operating costs of resale stores, agency and region headquarters, field operating activities, and support services. The primary revenue source for this activity group is a direct appropriation to the Defense WCF, which in turn transfers the funds to the DeCA WCF. Commissary Operations also receives additional revenues from manufacturers' coupon redemption fees, handling fees for tobacco products, and reimbursements for other support. DeCA receives an annual operating budget from DoD that establishes limitations for annual cost authority and annual capital expenditures for the two business areas.

DeCA's Surcharge Collections Trust Fund is funded primarily by a five percent surcharge applied to each sale. This fund, established by law, primarily finances DeCA's store-level information management equipment and support, and construction programs. The use of budgetary resources associated with the Surcharge Collections Trust Fund is limited by public law.

DeCA also receives minor amounts of military construction and procurement appropriated funds.

B. <u>Basis of Presentation and Accounting</u>

These financial statements have been prepared to report the financial position, net cost of operations, changes in net position, status and availability of budgetary resources, and the reconciliation between proprietary and budgetary accounts of DeCA. The Chief Financial Officers (CFO) Act of 1990, expanded by the Government Reform Act (GMRA) of 1994, requires DoD to prepare financial statements. DoD, in turn, requires DeCA to prepare audited financial statements. The financial statements have been prepared from the books and records of DeCA in accordance with accounting principles generally accepted in the United States of America and DoD accounting policies, which are summarized in this note. These financial statements, with the exception of the Statement of Budgetary Resources, are, therefore different from the financial management reports prepared by DeCA that are used to monitor and control DeCA's use of budgetary resources pursuant to Office of Management and Budget (OMB) directives.

Transactions are recorded on both an accrual accounting basis and a budgetary basis. Under the accrual method, revenues are recognized when earned, and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates compliance with legal requirements on the use of Federal funds. All material intra-agency transactions and balances have been eliminated for presentation on a consolidated basis. However, the Statement of Budgetary Resources is presented on a combined basis in accordance with OMB Circular A-136.

All dollar amounts are in thousands.

C. <u>Fund Balance with Treasury</u>

Fund balance with Treasury (FBWT) is the aggregate amount of funds in DeCA's accounts with the U.S. Department of Treasury (Treasury). FBWT primarily represents appropriated, revolving, and trust funds that are available to pay current liabilities and finance authorized purchases.

Note 2 provides specific, detailed information concerning FBWT.

D. <u>Cash</u>

Cash primarily consists of receipts from sales occurring during the last several days of the fiscal year that have been deposited into financial institutions, but are not yet credited to DeCA's FBWT.

E. <u>Accounts Receivable</u>

Accounts receivable consists of amounts owed to DeCA by other Federal agencies and the public. Federal accounts receivable arise generally from the provision of goods and services to other federal agencies. No allowance for doubtful accounts is determined for Federal accounts receivable.

Receivables from the public generally arise from the sale of grocery, meat, and produce items to authorized patrons. An allowance for doubtful accounts is established for reporting purposes based on past experience in the collection of accounts receivable and analysis of outstanding balances using the percentage of receivables. The allowance for loss on receivables account is adjusted accordingly at the time of collection or write-off during the fiscal year. Non-Federal accounts receivable are reported net of the allowance of $686 and $687 thousand as of September 30, 2005 and 2004, respectively.

F. Inventory

Inventory consisting primarily of grocery, meat, and produce items held for resale is stated at approximate cost as required by Statement of Federal Financial Accounting Standards (SFFAS) Number 3, *Accounting for Inventory & Related Property*.

G. General Property, Plant and Equipment

General property, plant and equipment (PP&E) consists of building, structures, and facilities (BSF), software, equipment, and construction-in-progress. PP&E is stated at acquisition cost, less accumulated depreciation. DoD establishes capitalization and depreciation policies for PP&E.

BSF is included in PP&E under DoD's "Preponderance of Use" policy. This policy recognizes that the DoD agencies that gain the most benefit by virtue of space usage should record the asset as general PP&E.

PP&E acquisitions are capitalized if the acquisition cost is $100,000 or more, and has a useful life of two or more years.

Depreciation is recognized on all PP&E, except construction-in-progress, on the straight-line basis over the estimated useful life of the asset. The useful lives are generally 40 years for buildings, structures, and facilities, and 5 years for software and equipment.

Note 3 provides specific, detailed information concerning General Property, Plant, and Equipment.

H. Other Liabilities

Other liabilities consist of payments DeCA owes to the Department of Labor (DOL) for workers' compensation paid under the Federal Employees Compensation Act (FECA), accrued payroll and benefits (including employer contributions and payroll taxes), foreign national separation pay, and accrued leave.

Workers' Compensation. FECA provides income and medical cost protection to covered Federal civilian employees injured on the job, employees who have incurred a work-related occupational disease, and beneficiaries of employees whose death is attributable to a job-related injury or occupational disease. DOL is responsible for administering the program and making payments for claims from eligible individuals. Subsequently, DOL bills Federal agencies for those claims from the individuals associated with the respective agency. The actuarially determined liability related to workers' compensation is described below.

Accrued Payroll and Benefits. Accrued payroll and benefits includes the portion of employee compensation earned, but not paid, at the end of the fiscal year along with DeCA's share of associated taxes, benefits, and retirement plan contributions.

Foreign National Separation Pay. DeCA operates in numerous foreign countries. These countries establish tariff agreements that outline certain employment terms and conditions related to its citizens. Under these tariff agreements, citizens for certain countries are entitled to special pay in the event their employment is terminated.

Accrued Leave. Federal employees' annual leave is accrued as it is earned. The accrual is reduced annually for actual leave taken and increased for leave earned. Each year, the accrued annual leave balance is also adjusted to reflect the latest pay rates. To the extent current or prior year appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future financing sources. DeCA employees can earn compensatory leave in lieu of overtime pay.

Note 4 provides specific, detailed information about Other Liabilities.

I. Actuarial Liability

In addition to the liabilities discussed above, DeCA records an actuarial liability for its remaining workers' compensation benefits. This liability, which is developed by DOL and provided to DoD after the end of each fiscal year, includes the expected future costs associated with death, disability, medical, and miscellaneous items for approved compensation cases. DOL determines the liability using a method that employs 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. The assumed interest rate for 10-year U.S. Treasury notes and bonds are 4.52 and 4.88 percent at September 30, 2005 and September 20, 2004, respectively. DoD uses a three-year moving average to distribute the actuarial liability to the various DoD agencies based on actual costs incurred by the respective DoD components.

J. Imputed Financing and Costs

DeCA recognizes imputed financing and costs related to Federal retirement plans, health benefits and life insurance and settlements paid by the U.S. Department of Treasury's Judgment Fund.

Retirement Plans. There are two primary retirement systems for Federal employees. Employees hired before January 1, 1984, may participate in the Civil Service Retirement System (CSRS). On January 1, 1984, the Federal Employees Retirement System (FERS) went into effect pursuant to Public Law 99-335. Most employees hired after December 31, 1983, are automatically covered by FERS and Social Security.

Employees hired before January 1, 1984, elected to either join FERS and Social Security or remain in CSRS. A primary feature of FERS is that it offers a savings plan to which DeCA automatically contributes one percent of pay and matches any employee contribution up to an additional four percent of pay. For most employees hired since December 31, 1983, DeCA also contributes the employer's matching share for Social Security.

DeCA does not report CSRS or FERS assets, accumulated plan benefits, or unfunded liabilities, if any, applicable to its employees. Reporting such amounts is the responsibility of the Office of Personnel Management (OPM) and FERS. DeCA recognizes imputed financing source and program expense for the difference between its contributions to Federal employee pension and other retirement benefits and the estimated actuarial costs as computed by the OPM.

Health Benefits and Life Insurance. The majority of DeCA employees are authorized to participate in the Federal Employees' Health Benefit (FEHB) program and the Federal Employees Group Life Insurance (FEGLI) program, which are administered by OPM. DeCA recognizes an imputed financing source and a program expense for these benefits.

Treasury Judgment Fund. Lawsuits settlements against DeCA may be paid by the Department of Treasury's Judgment Fund. DeCA recognizes an imputed financing source and a program expense for the amounts the Judgment Fund pays on behalf of DeCA.

K. Environmental Liabilities

DeCA's environmental liabilities reflect the potential liability associated with the clean-up and removal of environmentally hazardous materials, primarily asbestos, lead-based paint, polychlorinated biphenyls, and soil/water contamination, in DeCA's facilities. DeCA estimates its environmental liability based on the number of facilities constructed before 1988 that have not been remediated. The portion of the liability associated with those facilities with planned renovation projects during the next year are reported as current liabilities. The estimate is periodically adjusted upon completion of scheduled renovation projects. Actual costs may differ from the estimate due to possible changes resulting from inflation, deflation, technology, and/or applicable laws and regulations.

L. Net Position

Net position is the residual difference between assets and liabilities and comprises unexpended appropriations and cumulative results of operations.

Unexpended appropriations represent the amount of unobligated and unexpended budget authority. Unexpended appropriations are reduced for appropriations used and adjusted for other changes in budgetary resources, such as transfers and rescissions.

Cumulative results of operations represent the excess of revenues over expenses and transfers to the U.S. Treasury in the WCF since inception.

Note 5 provides specific, detailed information on Net Position.

M. Non-Exchange Revenue

DeCA recognizes non-exchange revenue for the labor received at no cost for local nationals working in the country of Japan. The Government of Japan pays the salary for local national employees up to a specified annual ceiling amount. Payroll over this ceiling is charged to the U.S. Government.

N. Use of Estimates

DeCA has made certain estimates and assumptions relating to the reporting of assets and liabilities, the disclosure of contingent liabilities, and the reporting of revenue and expenses in the financial statements. Actual results could differ from these estimates.

O. Reclassifications

Certain FY 2004 balances have been reclassified, retitled, or combined with other financial statement line items for consistency with current year presentation.

NOTE 2 - FUND BALANCE WITH TREASURY

FWBT consists of three types of funds – appropriated funds, revolving, and trust funds. Revolving funds involve DeCA's Resale fund, trust funds involve the Surcharge fund, and appropriated funds include commissary operations, military construction, and procurement funds.

The following table shows the balance for each type of fund as of September 30, 2005 and 2004:

Fund balances:	2005	2004
Appropriated funds	$ 233,476	$ 193,962
Revolving funds	59,154	78,443
Trust funds	209,533	177,963
Total	$ 502,163	$ 450,368

The following table shows the status of the fund balances as of September 30, 2005 and 2004:

Status of fund balances:	Appropriated	Revolving	Trust	Total
Unobligated balance available	$ 11,457	$ -	$ -	$ 11,457
Unobligated balance unavailable	15	-	-	15
Obligated balance not yet disbursed, net of contract authority	222,004	59,154	209,533	490,691
Total as of September 30, 2005	$ 233,476	$ 59,154	$ 209,533	$ 502,163

Status of fund balances:	Appropriated	Revolving	Trust	Total
Unobligated balance available	$ (27,140)	$ -	$ -	$ (27,140)
Unobligated balance unavailable	43	-	-	43
Obligated balance not yet disbursed, net of contract authority	221,059	78,443	177,963	447,465
Total as of September 30, 2004	$ 193,962	$ 78,443	$ 177,963	$ 420,368

The unobligated available fund balance as of September 30, 2004 is negative because obligations exceed budget authority. Effective October 1, 1998, the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) established new Treasury codes, referred to as subheads, for the two activity groups within DeCA's WCF. In conjunction with the establishment of the new Treasury codes, the OUSD(C) directed a transfer of net obligations, which were originally obligated under the old Treasury codes, to the Commissary Operations and Commissary Stock Resale activity groups. However, the OUSD(C) did not direct a transfer of the corresponding budget authority. In FY 2004, DeCA received a cash transfer from the Army, Navy, Air Force, and Defense-wide WCF accounts to DeCA's WCF account in the amount of $163.1 million to help correct this underfunding. As of September 30, 2005, DeCA reports a positive $11.4 million in unobligated balances available.

NOTE 3 - GENERAL PROPERTY, PLANT, AND EQUIPMENT

General property, plant, and equipment (PP&E) at September 30, 2005 and 2004 is summarized as follows:

PP&E category	Acquisition Value	Accumulated Depreciation	Net
Buildings, structures, and facilities	$ 1,812,264	$ (1,134,248)	$ 678,016
Software	9,660	(5,555)	4,105
Equipment and other assets	175,318	(126,989)	48,329
Construction-in-progress	74,464	-	74,464
Total as of September 30, 2005	$ 2,071,706	$ (1,266,792)	$ 804,914

PP&E category	Acquisition Value	Accumulated Depreciation	Net
Buildings, structures, and facilities	$ 1,777,774	$ (1,090,844)	$ 686,930
Software	9,422	(4,540)	4,882
Equipment and other assets	177,914	(112,363)	65,551
Construction-in-progress	68,424	-	68,424
Total as of September 30, 2004	$ 2,033,534	$ (1,207,747)	$ 825,787

DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS

NOTE 4 - LIABILITIES

The following table summarizes total liabilities covered and not covered by budgetary resources as of September 30, 2005 and 2004:

Intragovernmental:	**Covered by Budgetary Resources**	**Not Covered by Budgetary Resources**	**Total**
Accounts payable	$ 121,443	$ -	$ 121,443
Other	2,722	37,176	39,898
Subtotal	124,165	37,176	161,341
With the public:			
Accounts payable	447,293	-	447,293
Federal Employees Compensation Act actuarial liability	-	171,207	171,207
Environmental liabilities	-	31,866	31,866
Other	22,260	50,405	72,665
Subtotal	469,553	253,478	723,031
Total as of September 30, 2005	$ 593,718	$ 290,654	$ 884,372

Intragovernmental:	**Covered by Budgetary Resources**	**Not Covered by Budgetary Resources**	**Total**
Accounts payable	$ 150,753	$ -	$ 150,753
Other	2,385	37,591	39,976
Subtotal	153,138	37,591	190,729
With the public:			
Accounts payable	401,990	-	401,990
Federal Employees Compensation Act actuarial liability	-	174,076	174,076
Environmental liabilities	-	9,015	9,015
Other	33,018	49,816	82,834
Subtotal	435,008	232,907	667,915
Total as of September 30, 2004	$ 588,146	$ 270,498	$ 858,644

Other liabilities consist primarily of workers' compensation, accrued payroll and benefits, accrued unfunded annual and other leave, and foreign national separation pay. The following table summarizes other liabilities current and non-current as of September 30, 2005 and 2004.

Other liabilities	Current Liabilities	Non-Current Liabilities	Total
Intragovernment:			
Workers compensation	$ 15,938	$ 21,238	$ 37,176
Employer contributions and payroll taxes payable	2,722	-	2,722
Subtotal	18,660	21,238	39,898
With the public:			
Accrued funded payroll and benefits	22,260	-	22,260
Foreign national separation pay	12,336	-	12,336
Accrued unfunded annual leave	38,069	-	38,069
Subtotal	72,665	-	72,665
Total as of September 30, 2005	$ 91,325	$ 21,238	$ 112,563

Other liabilities	Current Liabilities	Non-Current Liabilities	Total
Intragovernment:			
Workers compensation	$ 16,696	$ 20,832	$ 37,528
Employer contributions and payroll taxes payable	2,385	-	2,385
Other	63	-	63
Subtotal	19,144	20,832	39,976
With the public:			
Accrued funded payroll and benefits	38,572	-	38,572
Foreign national separation pay	11,669	-	11,669
Accrued unfunded annual leave	38,147	-	38,147
Liability for deposit funds	(5,554)	-	(5,554)
Subtotal	82,834	-	82,834
Total as of September 30, 2004	$ 101,978	$ 20,832	$ 122,810

NOTE 5 - NET POSITION

The following table summarizes the net position by fund type as of September 30, 2005 and 2004:

Net position:	General Fund	Working Capital Fund	Total
Unexpended appropriations	$ 598	$ 49,786	$ 50,384
Cumulative results of operations	949,289	(65,204)	884,085
Total as of September 30, 2005	$ 949,887	$ (15,418)	$ 934,469

Net position:	General Fund	Working Capital Fund	Total
Unexpended appropriations	$ 345	$ 17,471	$ 17,816
Cumulative results of operations	950,018	(52,572)	897,446
Total as of September 30, 2004	$ 950,363	$ (35,101)	$ 915,262

NOTE 6 – INTRAGOVERNMENTAL COST

The Consolidated Statements of Net Cost reflects intragovernmental cost of $744,254 and $787,470 in fiscal years 2005 and 2004, respectively, related to operating expenses, such as the purchase of produce, non-capital equipment, transportation, and personnel costs from other Federal entities.

NOTE 7 – IMPUTED FINANCING

The imputed financing and cost for employee benefits for FY 2005 and 2004 is summarized below:

Benefit category	2005	2004
CSRS/FERS	$ 10,482	$ 11,141
FEHB	25,451	24,208
FEGLI	91	90
Other	4	1,209
Total	$ 36,028	$ 36,648

NOTE 8 - STATEMENTS OF CHANGES IN NET POSITION AND BUDGETARY RESOURCES

The Statement of Budgetary Resources is a combined statement and, as such, intra-entity transactions have not been eliminated. The combined Statement of Budgetary Resources has been prepared to coincide with the amounts shown in the President's Budget (Budget of the United States of America). However, the President's Budget is prepared from the Standard Form (SF) 133, Report on Budget Execution. Due to timing and the need for accelerated reporting at fiscal year end, the SF 133 is prepared using estimates, while the Statement of Budgetary Resources has been adjusted for actual results. As such, the FY 2005 Statement of Budgetary Resources may differ from the amounts in the President's Budget by the differences between estimates used for the SF 133 and the actual results reported in the Statement of Budgetary Resources.

The amounts reported in the FY 2004 Statement of Budgetary Resources are in agreement with the amounts reported for the DeCA Working Capital Fund of the President's Budget. The FY 2005 amounts will be available in the President's Budget during FY 2006. Both documents can be located at the OMB website (http://www.whitehouse.gov/omb).

As discussed in Note 2, DeCA has reported various amounts of negative unobligated balances at each fiscal year end through September 30, 2004. During fiscal year 2004, OUSD(C) transferred $163,100 from the Army, Navy, Air Force, and Defense-wide WCF accounts to DeCA's WCF account. In accordance with U.S. Standard General Ledger (USSGL) requirements, the transfer was initially recorded as an addition to cumulative results of operations. As the purpose of the transfer was to increase DeCA's overall budgetary resources and correct the negative unobligated balance situation, DeCA management recorded an equity transfer to reclassify the transfer from cumulative results of operations to unexpended appropriations.

Total budgetary resources in FY 2005 and FY 2004 consist primarily of spending authority from offsetting collections in the amount of $5,681,421 and $5,530,387, respectively, and an appropriation transfer from the Defense WCF in the amount of $1,174,609 and $1,089,482, respectively. The appropriation transfer is available indefinitely. Spending authority from offsetting collections results primarily from the sale of grocery, meat, and produce items.

Total budgetary resources in fiscal years 2005 and 2004 also include $16,071 and $9,466 of contract authority, respectively.

The obligated balance, net - end of period is comprised of the following components as of September 30, 2005 and 2004:

Obligated balance, net - end of period	**2005**	**2004**
Accounts receivable and cash	$ (144,672)	$ (144,813)
Unfilled customer order from Federal sources	(1,591)	(2,179)
Undelivered orders	325,664	304,355
Accounts payable and other liabilities	594,689	592,179
Total obligated balance, net - end of period	$ 774,090	$ 749,542

NOTE 9 - CONTINGENCIES

DeCA is a party in various administrative proceedings, legal actions and tort claims which may ultimately result in settlements or decisions adverse to the Federal government. DeCA has not accrued any amounts for contingent liabilities as the potential losses have not been determined to be probable and/or the amounts cannot be estimated. The amounts claimed related to the significant cases total approximately $1.3 million as of September 30, 2005.

DEFENSE COMMMISARY AGENCY
REQUIRED SUPPLEMENTARY INFORMATION
INTRAGOVERNMENTAL BALANCES
AS OF SEPTEMBER 30

Agency	Fund Balance with Treasury 2005	Fund Balance with Treasury 2004	Accounts Receivable 2005	Accounts Receivable 2004
Department of Treasury	$ 502,163	$ 450,368	$ -	$ -
Department of State	-	-	211	103
Department of Defense	-	-	328	149
Total	$ 502,163	$ 450,368	$ 539	$ 252

Agency	Accounts Payable 2005	Accounts Payable 2004	Other Liabilities 2005	Other Liabilities 2004
Department of Treasury	$ 7,600	$ 1,487	$ -	$ 63
Department of Labor	-	-	37,176	37,528
General services Administration	3,080	5,099	-	-
Department of Defense	109,705	143,114	-	-
Office of Personnel Management	747	593	2,722	2,385
Other	311	460	-	-
Total	$ 121,443	$ 150,753	$ 39,898	$ 39,976

Agency	Expenses 2005	Expenses 2004	Revenue 2005	Revenue 2004
Department of Treasury	$ 7,744	$ 1,774	$ -	$ -
Department of State	553	-	979	1,195
Department of Labor	16,344	16,232	-	-
Department of Homeland Security	-	86	1,551	1,608
General Services Administration	11,275	21,529	-	-
Department of Defense	593,962	639,961	7,236	1,129
Department of Veteran Affairs	4,589	-	-	-
NASA	439	1,400	-	-
Office of Personnel Management	108,921	104,770	-	-
Other	427	1,718	-	-
Total	$ 744,254	$ 787,470	$ 9,766	$ 3,932

DEFENSE COMMMISARY AGENCY
REQUIRED SUPPLEMENTARY INFORMATION
COMBINING STATEMENT OF BUDGETARY RESOURCES
FOR THE YEAR ENDED SEPTEMBER 30, 2005

	Defense Working Capital Funds			General Funds			
	Operations	Resale	Other	Surcharge	Military Construction	Procurement	Combined
Budgetary resources							
Budget authority	$ 1,178,958	$ 10,421	$ -	$ -	$ 399	$ -	$ 1,189,778
Unobligated balance brought forward	(27,279)	-	-	-	154	28	(27,097)
Net transfers and adjustments	729	-	-	-	-	(28)	701
Spending authority from offsetting collections	24,957	5,373,193	(27)	283,298	-	-	5,681,421
Recoveries of prior year obligations	1,297	6,949	-	4,163	112	-	12,521
Permanently not available	-	-	-	(4,492)	(112)	-	(4,604)
Total budgetary resources	$ 1,178,662	$ 5,390,563	$ (27)	$ 282,969	$ 553	$ -	$ 6,852,720
Status of budgetary resources							
Obligations incurred							
Direct	$ 1,142,022	$ -	$ -	$ -	$ 447	$ -	$ 1,142,469
Reimbursable	25,274	5,390,563	(27)	282,969	-	-	5,698,779
Total obligations incurred	1,167,296	5,390,563	(27)	282,969	447	-	6,841,248
Unobligated balances	11,366	-	-	-	106		11,472
Total status of budgetary resources	$ 1,178,662	$ 5,390,563	$ (27)	$ 282,969	$ 553	$ -	$ 6,852,720
Relationship of obligations to outlays							
Obligated balance, net - beginning of period	$ 244,250	$ 233,520	$ 9,378	$ 262,112	$ 282	$ -	$ 749,542
Total obligations incurred	1,167,296	5,390,563	(27)	282,969	447	-	6,841,248
Less: spending authority from offsetting collections and recoveries of prior year obligations	(26,254)	(5,380,142)	27	(287,461)	(112)	-	(5,693,942)
Obligated balance, net - end of period	(250,371)	(224,769)	(9,262)	(289,189)	(499)	-	(774,090)
Total outlays	$ 1,134,921	$ 19,172	$ 116	$ (31,569)	$ 118	$ -	$ 1,122,758
Outlays							
Disbursements	$ 1,158,395	$ 5,390,154	$ 116	$ 256,124	$ 118	$ -	$ 6,804,907
Collections	(23,474)	(5,370,982)	-	(287,693)	-	-	(5,682,149)
Total outlays	$ 1,134,921	$ 19,172	$ 116	$ (31,569)	$ 118	$ -	$ 1,122,758

DEFENSE COMMMISARY AGENCY
REQUIRED SUPPLEMENTARY INFORMATION
COMBINING STATEMENT OF BUDGETARY RESOURCES
FOR THE YEAR ENDED SEPTEMBER 30, 2004

	Defense Working Capital Funds			General Funds			
	Operations	Resale	Other	Surcharge	Military Construction	Procurement	Combined
Budgetary resources							
Budget authority	$ 1,097,046	$ 1,666	$ -	$ -	$ 236	$ -	$ 1,098,948
Unobligated balance brought forward	(193,702)	-	-	-	88	28	(193,586)
Net transfers and adjustments	163,100	-	-	-	73	-	163,173
Spending authority from offsetting collections	26,006	5,234,837	-	269,544	-	-	5,530,387
Recoveries of prior year obligations	12,774	8,476	-	103	-	-	21,353
Permanently not available	-	-	-	(10,167)	-	-	(10,167)
Total budgetary resources	$ 1,105,224	$ 5,244,979	$ -	$ 259,480	$ 397	$ 28	$ 6,610,108
Status of budgetary resources							
Obligations incurred							
Direct	$ 1,106,508	$ -	$ -	$ -	$ 243	$ -	$ 1,106,751
Reimbursable	25,995	5,244,979	-	259,480	-	-	5,530,454
Total obligations incurred	1,132,503	5,244,979	-	259,480	243	-	6,637,205
Unobligated balances	(27,279)	-	-	-	154	28	(27,097)
Total status of budgetary resources	$ 1,105,224	$ 5,244,979	$ -	$ 259,480	$ 397	$ 28	$ 6,610,108
Relationship of obligations to outlays							
Obligated balance, net - beginning of period	$ 271,465	$ 196,841	$ 8,033	$ 270,573	$ (486)	$ -	$ 746,426
Total obligations incurred	1,132,503	5,244,979	-	259,480	243	-	6,637,205
Less: spending authority from offsetting collections and recoveries of prior year obligations	(38,780)	(5,243,313)	-	(269,647)	-	-	(5,551,740)
Obligated balance, net - end of period	(244,250)	(233,520)	(9,378)	(262,112)	(282)	-	(749,542)
Total outlays	$ 1,120,938	$ (35,013)	$ (1,345)	$ (1,706)	$ (525)	$ -	$ 1,082,349
Outlays							
Disbursements	$ 1,149,187	$ 5,224,743	$ (132)	$ 266,395	$ (525)	$ -	$ 6,639,668
Collections	(28,249)	(5,259,756)	(1,213)	(268,101)	-	-	(5,557,319)
Total outlays	$ 1,120,938	$ (35,013)	$ (1,345)	$ (1,706)	$ (525)	$ -	$ 1,082,349

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KPMG LLP
2001 M Street, NW
Washington, DC 20036

Independent Auditors' Report

Audit Committee
Defense Commissary Agency:

We have audited the accompanying consolidated balance sheets of the Defense Commissary Agency (DeCA) as of September 30, 2005 and 2004, and the related consolidated statements of net cost, changes in net position, and financing and combined statements of budgetary resources for the years then ended. The objective of our audits was to express an opinion on the fair presentation of these financial statements. In connection with our audits, we also considered DeCA's internal control over financial reporting and tested DeCA's compliance with certain provisions of applicable laws and regulations that could have a direct and material effect on these financial statements.

SUMMARY

As stated in our opinion on the financial statements, we concluded that DeCA's financial statements as of and for the years ended September 30, 2005 and 2004, are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America.

Our consideration of internal control over financial reporting resulted in the following conditions being identified as reportable conditions:

- ***Property, Plant, and Equipment.*** DeCA's controls over the accountability and record keeping of its capitalized and non-capitalized equipment.
- ***Information Technology.*** The general and application controls associated with DeCA's financial and financial-related systems continue to need improvement.

However, these reportable conditions are not believed to be material weaknesses.

The results of our tests of compliance with certain provisions of laws and regulations, exclusive of those referred to in the *Federal Financial Management Improvement Act of 1996* (FFMIA), disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards,* issued by the Comptroller General of the United States, or Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements.*

The results of our tests of FFMIA disclosed instances where DeCA's financial management systems did not substantially comply with Federal financial management system requirements, and were not compliant with the U.S. Standard General Ledger at the transaction level.

The results of our tests of FFMIA disclosed no instances in which DeCA's financial management systems did not substantially comply with Federal accounting standards.

The following sections discuss our opinion on DeCA's financial statements, our consideration of DeCA's internal control over financial reporting, our tests of DeCA's compliance with certain provisions of applicable laws and regulations, and management's and our responsibilities.

OPINION ON THE FINANCIAL STATEMENTS

We have audited the accompanying consolidated balance sheets of the Defense Commissary Agency as of September 30, 2005 and 2004, and the related consolidated statements of net cost, changes in net position and financing, and combined statements of budgetary resources for the years then ended.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of DeCA as of September 30, 2005 and 2004, and its net costs, changes in net position, budgetary resources, and reconciliation of net costs to budgetary obligations, for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The information in the Management's Discussion and Analysis and Performance Sections and the required supplementary information on pages 1 to 26 and 45 to 47 is not a required part of the financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America or OMB Circular A-136, *Financial Reporting Requirements*, Part A, *Form and Content of the Performance and Accountability Report*. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information and, accordingly, we express no opinion on it.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect DeCA's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements.

Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

In our fiscal year 2005 audit, we noted certain matters, described in Exhibit 1, involving internal control over financial reporting and its operation that we consider to be reportable conditions. However, none of the reportable conditions are believed to be material weaknesses.

* * * * *

A summary of the status of prior year reportable conditions is included as Exhibit 2.

We also noted certain additional matters that we reported to the management of DeCA in a separate letter.

COMPLIANCE AND OTHER MATTERS

Our tests of compliance with certain provisions of laws and regulations, as described in the Responsibilities section of this report, exclusive of those referred to in the *Federal Financial Management Improvement Act of 1996* (FFMIA), disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-2.

The results of our tests of FFMIA disclosed instances, described in Exhibit 3, where DeCA's financial management systems did not substantially comply with Federal system requirements, and were not compliant with the United States Standard General Ledger at the transaction level.

RESPONSIBILITIES

Management's Responsibilities

The *Government Management Reform Act of 1994* (GMRA), *Accountability of Tax Dollars Act, and Government Corporation Control Act* require agencies to report annually to Congress on their financial status and any other information needed to fairly present their financial position and results of operations. To assist the Department of Defense in meeting these requirements, DeCA prepares and submits financial statements in accordance with Part A of OMB Circular A-136.

Management is responsible for the financial statements, including:

- Preparing the financial statements in conformity with accounting principles generally accepted in the United States of America;
- Preparing the Management Discussion and Analysis (including the performance measures) and Required Supplementary Information;
- Establishing and maintaining internal controls over financial reporting; and
- Complying with laws and regulations, including FFMIA.

In fulfilling this responsibility, management is required to make estimates and judgments to assess the expected benefits and related costs of internal control policies. Because of inherent limitations in internal control, misstatements due to error or fraud may nevertheless occur and not be detected.

Auditors' Responsibilities

Our responsibility is to express an opinion on the fiscal year 2005 and 2004 financial statements of DeCA based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, and OMB Bulletin No. 01-02. Those standards and OMB Bulletin No. 01-02 require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of DeCA's internal control over financial reporting. Accordingly, we express no such opinion.

An audit also includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall financial statement presentation.

We believe that our audits provide a reasonable basis for our opinion.

In planning and performing our fiscal year 2005 audit, we considered DeCA's internal control over financial reporting by obtaining an understanding of DeCA's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in *Government Auditing Standards* and OMB Bulletin No. 01-02. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*. The objective of our audit was not to provide assurance on DeCA's internal control over financial reporting. Consequently, we do not provide an opinion thereon.

As further required by OMB Bulletin No. 01-02, in our fiscal year 2005 audit, with respect to internal control related to performance measures determined by management to be key and reported in the Management's Discussion and Analysis and Performance sections, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions. Our procedures were not designed to provide assurance on internal control over reported performance measures and, accordingly, we do not provide an opinion thereon.

As part of obtaining reasonable assurance about whether DeCA's fiscal year 2005 financial statements are free of material misstatement, we performed tests of DeCA's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 01-02, including certain provisions referred to in FFMIA. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws and regulations not applicable to DeCA. However, providing an opinion on compliance with laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

Under OMB Bulletin No. 01-02 and FFMIA, we are required to report whether DeCA's financial management systems substantially comply with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements.

DISTRIBUTION

This report is intended for the information and use of DeCA's management, the Department of Defense, OMB, the Government Accountability Office, and the U.S. Congress, and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

October 31, 2005

Reportable Conditions

Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect DeCA's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements.

We consider the following to be reportable conditions.

Property, Plant, and Equipment

Condition

DeCA does not have adequate policies and procedures in place to ensure the proper accountability and record keeping of its capitalized and non-capitalized equipment.

Discussion

Improvements in the accountability of non-capital and capital equipment have been made by DeCA's Property Record Management Office. However, significant deficiencies still exist. Specifically, DeCA does not:

- have effective operating procedures in place to require thorough, periodic reviews of DeCA's property database, the Defense Property Accountability System (DPAS);
- conduct effective reviews of the property database to ensure register components, which are DeCA's most significant class of capital assets, are properly recorded among DeCA locations; and
- have effective operating procedures in place to ensure register component replacements or transfers between locations are properly recorded as capital equipment.

As a result of our audit tests, we found that 117 commissaries had different numbers of register components recorded as capital equipment than the number of register systems on hand at the commissary.

In addition, DeCA personnel conduct an annual physical inventory of all capital equipment. During our review of these annual physical inventories, we found that DeCA does not have effective procedures or resources to conduct a thorough and complete reconciliation of its physical inventory results prior to the end of the fiscal year. Specifically, we noted the following errors which were corrected by DeCA personnel prior to the preparation of its annual financial statements:

- 9 instances in which the property items found during the physical inventory were not appropriately added to the property records.
- 13 instances in which the property items not located during the physical inventory were not appropriately removed from the property records.
- 38 instances in which changes noted by the store personnel while performing the physical inventory, such as changes to serial numbers, bar codes, and/or locations, were not appropriately updated in the property records.

(Continued)

Criteria

- Department of Defense Financial Management Regulation, volume 4, chapter 6, *Property, Plant, and Equipment,* states that personal property with a life of at least two years and a cost of $100,000 must be capitalized. Prior to fiscal year 1996, the capitalization threshold was less than $100,000 and varied according to the year that the item was acquired. Such property shall remain capitalized.
- Department of Defense Financial Management Regulation, volume 4, chapter 1, *Financial Control of Assets*, states that assets shall be under continuous accounting control from acquisition to disposition. Such control helps ensure proper and authorized use as well as adequate care and preservation, since no asset can be acquired, put into use, transferred, written down, or disposed of, without proper authorization necessary to document and record the transaction.

Recommendation

We recommend that DeCA:

- Develop and implement effective policies and procedures to conduct thorough reviews and reconciliations of the personal property records. These reviews may consist of reviewing property records for capital equipment recorded as non-capital equipment, reviewing store property records for unequal register system components, and any additional reviews that may detect other abnormalities in the property listing.
- Perform a complete review of register system components reported as capital equipment. Determine the cause for unequal components and train employees appropriately in order to avoid differences from occurring in the future.
- Perform a complete review of register system components reported as non-capital equipment. Determine the appropriateness for recording as non-capital and if necessary immediately adjust those items from non-capital to capital equipment.
- Develop and implement effective policies and procedures to ensure register component replacements and transfers between stores are appropriately recorded as capital equipment, when necessary.
- Develop written procedures and guidance for the conduct of accountable inventories by store and region personnel. Ensure accountable inventories are completed during the appropriate time period to allow for adequate reconciliations of the inventory results.

Management Response

DeCA concurs that additional processes, policies, and training changes are needed to improve equipment accountability throughout DeCA. Based on additional research performed by the Property Record Management Office (PRMO), DeCA was able to reduce the number of commissaries with incomplete register system components to 17 locations as of October 13, 2005. The estimated completion for additional reviews is January 2006. PRMO is also coordinating with Resource Management to ensure that register components are properly recorded as capital equipment and will make changes as appropriate. In addition, completion of training for headquarters, regions, zones, stores, and central distribution centers is estimated for March 2006.

(Continued)

Information Technology

Condition

The general and application controls associated with DeCA's financial systems continue to need improvement. Due to the sensitive nature of the issues identified, we will provide DeCA officials with a separate, restricted distribution report, which contains the detailed results of our review, along with specific recommendations.

Discussion

As part of our fiscal year 2005 audit of DeCA's financial statements, we performed review of information technology application controls over the following key DeCA applications that support financial transactions and reporting:

- DeCA Interactive Business System (DIBS);
- Electronic Data Interchange (EDI);
- Standard Automated Voucher Examination System (SAVES);
- Accounting and Inventory Management System (AIMS);
- Point of Sale – Technical Refresh (POS-TR); and
- Pick ticket Warehouse Management System (PkMS).

We also performed a follow-up to our prior year limited applications controls review over those applications owned and operated by other DoD components that support DeCA financial transactions and reporting. These applications included:

- Defense Business Management System (DBMS);
- Standard Financial System (STANFINS);
- Columbus Cash Accountability System (CCAS);
- Defense Property Accountability System (DPAS);
- Modern Defense Civilian Personnel Data System (Modern DCPDS); and
- Defense Civilian Payroll System (DCPS).

We conducted our review during the period May 2005 to August 2005. Our separate report will identify internal control weaknesses for the financial systems that require management attention. We will also provide management with an evaluation of the current status of previously identified information technology vulnerabilities.

(Continued)

Exhibit 1

Criteria

We performed our review in compliance with guidance established in the Government Accountability Office's *Financial Audit Manual* and *Federal Information System Controls Audit Manual*. We also used the following Federal and DoD security guidelines as criteria for determining whether controls were in place and operating as intended:

- OMB Circular Number A-130, Management of Federal Information Resources;
- OMB Circular Number A-127, Financial Management Systems;
- OMB Circular Number A-123, Management Accountability and Control;
- Public Law 100-235, The Computer Security Act of 1987;
- National Institute of Standards and Technologies (NIST) publications;
- DoD Instruction 8500.2, Information Assurance Implementation;
- DoD Directive 5200.28, Security Requirements for Automated Information Systems;
- DoD 5200.28-STD, Department of Defense Trusted Computer System Evaluation Criteria; and
- DoD Instruction 5200.4, DoD Information Technology Security Certification and Accreditation Process (DITSCAP).

Recommendation

Due to the sensitive nature of these findings, our separate report will recommend that DeCA management implement certain procedures to address the application control vulnerability of its financial systems.

Management Response

Management's responses will be included in the separate report.

Exhibit 2

Status of Prior Year Reportable Conditions

Area	Status as of September 30, 2004	Status as of September 30, 2005
Property, Plant, and Equipment	**Reportable Condition:** DeCA does not have adequate policies and procedures in place to ensure the proper accountability and record-keeping of its capitalized and non-capitalized equipment.	**Continue as reportable condition:** Improvements have been made to resolve some weaknesses noted in the prior year. However, significant deficiencies still exist to ensure the proper accountability and record-keeping of capitalized and non-capitalized equipment.
Information Technology	**Reportable Condition:** The general and application controls associated with DeCA's financial and financial-related systems continue to need improvement.	**Continue as a reportable condition:** Improvements have been made to resolve some weaknesses noted in the prior year. However, significant effort must be made to resolve security and access control weaknesses over key systems.

Exhibit 3

Compliance with Laws and Regulations

This section discusses issues related to noncompliance with laws and regulations that could have a material impact on DeCA's financial statements.

Federal Financial Management Improvement Act of 1996 (FFMIA)

Condition

We again noted that DeCA was not in substantial compliance with FFMIA.

Discussion

DFAS uses two separate accounting systems to process DeCA transactions. DBMS accounts for transactions associated with the appropriated funds and surcharge collections and STANFINS accounts for all resale inventory transactions. In addition, STANFINS does not interface with DBMS. Thus, there are two core accounting systems that DFAS uses to account for DeCA transactions. Since these systems do not interface, DeCA is not in compliance with Federal financial management system requirements, which call for a single, integrated financial system.

In addition, both STANFINS and DBMS are not compliant with the U.S. Standard General Ledger. Neither system is able to process transactions in accordance with the U.S. Standard General Ledger at the detail level, and extensive manual processes are required to adjust STANFINS and DBMS balances to allow for compilation of DeCA's financial statements. For example, DBMS does not contain a general ledger account to record unexpended appropriation transfers. DFAS-CO and DeCA personnel must use a combination of information inside and outside of DBMS to calculate unexpended appropriation transfers at the end of each reporting period.

Criteria

FFMIA requires that an agency's financial management systems substantially comply with Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger at the transaction level.

Recommendation

We again recommend that DeCA continue to work with DFAS to implement actions to comply with the requirements of FFMIA.

Management Response

DeCA will continue to work with DFAS and other DoD components to implement appropriate changes in policies, procedures, and systems in order to satisfy requirements of FFMIA by FY 2007.

DEFENSE COMMISSARY AGENCY
HEADQUARTERS
1300 E AVENUE
FORT LEE, VIRGINIA 23801-1800

REPLY TO
ATTENTION OF

IG

October 20, 2005

MEMORANDUM FOR CHIEF EXECUTIVE OFFICER

SUBJECT: Summary of Serious Management and Performance Challenges

OMB memorandum dated October 18, 2002, and OMB memorandum M-03-13 dated May 21, 2003, requires this office provide you with the Inspector General (IG) perspective on the most serious management and performance challenges facing DeCA for inclusion in the Agency's annual *Performance and Accountability Report.*

The *Reports Consolidation Act of 2000 (Public Law 106-531)* left the determination and threshold of what constitutes a most serious management challenge to the discretion of the Inspectors General. As a result, I applied the following definition in preparing the statement for 2005:

Serious management challenges are mission critical areas or programs that have the potential for a perennial vulnerability that, without substantial management attention, would seriously impact Agency operations or strategic goals vital to the Agency's mission.

This office believes that by regularly addressing challenges surrounding these issues DeCA can enhance program efficiency and effectiveness; avoid potential operational and financial problems; and decrease fraud, waste, abuse and mismanagement.

Information Technology (IT) Security & Management

DeCA's Information Systems Management and Control is critical to delivery of the benefit. Our **FY 2005 Federal Information Security Management Act (FISMA)**[1] review found that DeCA FISMA compliance improved over FY 2004, despite additional Department requirements, and the Agency's progress should again cause it to receive excellent information assurance grades on certification and accreditation, security configuration, and incident detection/reporting from the Department. DeCA has received extensive IT audit coverage from DoDIG, DISA, KPMG (DeCA's external auditor) and DeCA-IR. The Office of the Inspector General (OIG) believes this area has improved, but must be tested through the use of regular internal management controls. The DeCA OIG intends to review quarterly in FY 2006 the key management review items at risk and the IT corrective action taken on issues identified and report on review results.

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[1] FISMA provides a comprehensive framework for ensuring that information resources supporting Federal operations and assets employ effective security controls. FISMA requires agencies to conduct annual information security program reviews and Offices of the Inspector General to perform independent evaluations of those programs.

The key to DeCA's future mission accomplishment lies largely in its ability to meet the challenge of successfully deploying the Commissary Advanced Resale Transaction System (CARTS) and resolving existing IT Help Desk "first call" anomalies. CARTS, a DeCA PEO responsibility, is critically tied to the IT community. The Agency assured CARTS complied with DoD's Business Management Modernization Program (BMMP) in order to instill discipline and management of the CARTS purchase and subsequent interface with legacy replacement and new requirement systems from an enterprise perspective. The Agency chartered two *Lean Six Sigma* (L6S) projects with the launch of the IT Help Desk Team Project and the IT Process Flow Team Project with the intent to improve information flow processes.

Financial Management

DeCA received a reasonable assurance statement from its external auditor for FY 2004 that it's financial and performance reporting was reliable with no material weaknesses found. The DeCA Chief Financial Executive reports that preliminary discussions with our external auditors indicate the same results probable for FY 2005.

Plant, Property, Equipment Program Management

Plant, property and equipment management were of special interest to DeCA's external auditor (KPMG) and the OIG in FY 2005. The Operations, Planning and Comptroller community improved Agency performance in FY 2005 by reducing program inventory accountability differences in the system. Book to actual physical inventory difference amounts were reduced from $40M in FY 2004 to $8.5M for FY 2005. The Agency made this item a number one priority for improvement by chartering a L6S Equipment Inventory Project Team to improve the process and thereby further reduce un-reconciled amounts and help prevent recurring problems. The challenge will be in guiding the L6S business transformation effort to ensure broad based cooperation, functional process ownership, and accountability in order to ensure future data integrity and resolve the $8.5M inventory difference.

Internal Controls

At the benefit delivery level the OIG tested 15 percent (40) of all commissaries in FY 2005 and found there continued to be regulatory compliance improvement. The FY 2005 average unannounced inspection score was 81.1 percent or almost two percent better than FY 2004. The OIG tested regulatory compliance at 25 percent of the Agency's Central Distribution Centers (CDCs) and found an average compliance rating score of 74.2 percent on all items tested. This was a 30 percent improvement over FY 2004. As of September 28, management reported that 94.6 percent of reportable IG findings had been corrected. At Region Directors' requests, the OIG conducted Staff Assistance Visits at five additional commissaries where the effectiveness of existing internal controls was measured. DeCA's challenge in FY 2006 will be to ensure the Agency complies with the new financial control requirements of **OMB Circular Number A-123, Appendix A** and its related OSD guidance in mission critical and target rich abuse areas.

Human Capital Management

As of September 30, DeCA had approximately 18,000 employees worldwide. There were an additional 118 contractors at Headquarters DeCA. The Agency challenges in human capital are multifaceted. DeCA must ensure its future civilian and contractor workforces are rightly sized, multi-skilled to function in an integrated and less hierarchical environment, capable of prudent and intelligent risk taking in safe surroundings while dealing with 2005 BRAC actions and emerging technological factors. DeCA started the centralization of many functional processes and thus reduced and flattened its organizational structure and staff in FY 2005 with Commissary Operating Board (COB) and field operations concurrence. DeCA plans to continue its transformation in this area through business case justification and by becoming the employer of choice while fostering a professional growth culture based on DeCA values of leadership and integrity.

Personnel issues were the major FWA investigation and assistance item in FY 2005 and represented 27 percent of all issues/complaints/allegations received. The OIG database also revealed that 47 percent of all congressional inquires concerned DeCA employee personnel issues. The percentage of individual administrative wrongdoing allegations that were substantiated for closed cases received in FY 2005 was higher than the substantiation rate at the DoDIG Hotline level. However, this was primarily due to better inquiry officer training that allowed only true and credible allegations to be subject to investigation. The total number of OIG allegations, complaints, issues, contacts and referrals received in FY 2005 declined by 18.5 percent over FY 2004 and was the lowest FY number ever received by the DeCA OIG.

John T. Maffei
Inspector General

Glossary of Acronyms

ACSI – American Customer Satisfaction Index

CCSS – Commissary Customer Service Survey

COB – Commissary Operating Board

COOP – Contingency Operations Plan

DeCA – Defense Commissary Agency

DITSCAP – DoD Information Technology Security Certification and Accreditation Process

DoD – Department of Defense

DoL – Department of Labor

DPAS – Defense Property Accounting System

DWCF – Defense Working Capital Fund

EDI – Electronic Data Interchange

FBWT – Fund Balance With Treasury

FCI – Facility Condition Index

FECA – Federal Employees Compensation Act

FFMIA – Federal Financial Management Improvement Act of 1996

FMFIA – Federal Managers' Financial Integrity Act

FTE – Full Time Equivalent

GAO – Government Accountability Office

IPT - Integrated Process Team

KPMG – (Independent Audit Firm)

LIFE - Leadership – Integrity – Flexibility – Enjoyment

MD&A – Management Discussion and Analysis

OMB – Office of Management and Budget

OSD (P&R) - Office of Secretary of Defense (Personnel & Readiness)

PA&E – Program Analysis and Evaluation

PBD – Program Budget Decision

PMA – President Management Agenda

POS – Point of Sale

PPBE – Planning, Programming, Budgeting and Execution

PP&E – Property, Plant and Equipment

SES – Senior Executive Service

UPC – Universal Product Code

USD(C) – Under Secretary of Defense (Comptroller)

WCF – Working Capital Fund

ACSI – American Customer Satisfaction Index