



ACQUISITION,
TECHNOLOGY
AND LOGISTICS

THE UNDER SECRETARY OF DEFENSE

3010 DEFENSE PENTAGON
WASHINGTON, DC 20301-3010

JUN 1 2 2007

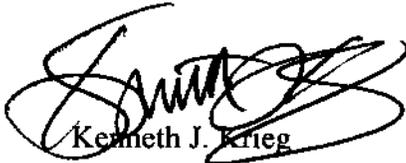
MEMORANDUM FOR SECRETARIES OF THE MILITARY DEPARTMENTS
COMMANDER, U.S. SPECIAL OPERATIONS COMMAND
DIRECTORS OF THE DEFENSE AGENCIES

SUBJECT: Implementation of Proper Financial Accounting Treatment for Military
Equipment

I commend and thank you for your efforts on the Military Equipment Valuation and Accountability (MEVA) initiative. Due to your efforts, the Department of Defense established a baseline of military equipment (ME) on October 4, 2006 with ME baseline values as of September 30, 2006. As a step toward further compliance with Statement of Federal Financial Accounting Standards (SFFAS) No. 6, "Accounting for Property, Plant, and Equipment," my June 30, 2006, memorandum (Attachment 1), "Proper Financial Accounting Treatment for Military Equipment," addresses the requirement to separately identify requisition and contract line items to ensure the proper treatment and allocation of program expenditures between capitalized assets and expenses. Guidance on the military equipment definition and current capitalization thresholds for military equipment, which were revised since publication of the memorandum, may be found at <http://www.acq.osd.mil/me/reflib.html>.

As we move forward, I would like your assessment of how the policy is being implemented within your organization. Your assessment should include lessons-learned, barriers to implementation, and potential measures of effectiveness. I would expect to see improvements, changes, and corrective actions incorporated into your military equipment key milestone plan. Using the attached self-assessment questionnaire (Attachment 2), please provide me a summary of your assessments by August 1, 2007. Beginning December 31, 2007, please report quarterly on the effectiveness of this policy using the measures we agree on.

My point of contact is Mr. Richard K. Sylvester, Deputy Director for Property and Equipment Policy. He can be reached at 703-604-6350 ext 121 or at richard.sylvester@osd.mil.



Kenneth J. Krieg

Attachments:
As Stated

cc: DoD OIG
DCFO





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MEMORANDUM FOR SECRETARIES OF THE MILITARY DEPARTMENTS COMMANDER, U.S. SPECIAL OPERATIONS COMMAND DIRECTORS OF THE DEFENSE AGENCIES

SUBJECT: Proper Financial Accounting Treatment for Military Equipment

Military Equipment (ME) valuation is a Department of Defense (DoD) initiative to value, capitalize, and depreciate equipment to meet Federal accounting standards. DoD has made great progress in establishing a baseline value for ME acquired prior to Fiscal Year (FY) 2006. On October 1, 2006, the focus of ME valuation will shift to compliance with an even more rigorous accounting standard, Statement of Federal Financial Accounting Standards (SFFAS) No. 6, "Accounting for Property, Plant, and Equipment." Fundamental changes in our acquisition business processes will be required to identify the proper accounting treatment and allocation of program expenditures between capitalized assets and expenses.

To implement this SFFAS requirement, program managers, business/financial management analysts, and contracting personnel, for every program, project, product, or system that has deliverable end items which meet the requirements for capitalization as equipment, will be required to separately identify requisition and contract line items to ensure the proper treatment and allocation of program expenditures between capitalized assets and expenses. This change in acquisition process is critical for meeting the Department's goal of achieving knowledge enabled business.

Attached is guidance on how to implement the new business processes. These changes are mandatory and will be effective for contracts and orders to be awarded on and after October 1, 2006. If you have any questions, or need additional information, please contact Mr. Richard K. Sylvester, in the Property and Equipment Policy Office. He can be reached at 703-604-6350 ext 121 or via e-mail at richard.sylvester@osd.mil.



Kenneth J. Krieg

Attachments:

As stated

cc:

DoD OIG

DCFO



Military Equipment Defined: Military equipment are tangible assets that:

1. Have an estimated useful life of 2 or more years;
2. Are not intended for sale;
3. Are intended to be used or available for use in the performance of military missions, to include equipment used in training; and
4. Meet capitalization threshold as defined in the DoD Financial Management Regulation (FMR) Volume 4, Chapter 6 located at http://www.dod.mil/comptroller/fmr/04/04_06.pdf. This threshold is currently a unit cost of \$100,000 or greater.

Examples of military equipment are aircraft, ballistic missiles, communications and electronic devices and systems, satellites, combat ships, support ships, and combat vehicles. These are assets that were previously defined as National Defense Property, Plant and Equipment (PP&E) under Statement of Federal Financial Accounting Standards (SFFAS) No. 11.

Training and Guidance: Planning for the FY 2007 contracts is already underway and representatives of the Property and Equipment Policy (P&EP) Office, OUSD(AT&L), are developing detailed guidance, continuous learning modules, and training that will be provided at each systems command that has begun in April 2006 to assist all elements of the finance, acquisition, logistics and contracting communities to meet their responsibilities relative to these new requirements. This guidance and training will be posted on the military equipment website located at <http://www.acq.osd.mil/me/index.htm>. The purpose of this additional guidance and training will be to answer questions and give examples of the changes contained within this attachment.

Program Managers: To implement this initiative, the program managers for any program, project, product, or system that has deliverable end items that meet the capitalization threshold must prepare a program description as part of the acquisition strategy at Milestone C (or any other decision point that leads to production or procurement of end items to be used for operations). Detailed guidance on the capitalization threshold may be found in the DoD Financial Management Regulation (FMR) Volume 4, Chapter 6 located at http://www.dod.mil/comptroller/fmr/04/04_06.pdf.

The program description should identify the following deliverables:

- The end item(s) meeting the capitalization thresholds;
 - The government furnished material that will be included in the end item(s);
 - Other deliverables that will accompany the end item (e.g., manuals, tech data, etc.);
- and

Proper Financial Accounting Treatment for Military Equipment Valuation

- Other types of deliverables that will be bought with program funding (e.g., initial spares, support equipment, special tooling and test equipment, etc.), but that cannot be directly attributed to a specific end item.

This program description should be consistent with level 2 of the Program Work Breakdown Structure (WBS) as described in MIL_HDBK-881A. The information will be provided as an attachment to the Acquisition Strategy Report required by DoD 5000.2 until an Acquisition Program Unique Identification (APUID) Registry is established. The APUID, when implemented, will replace and expand the current Program Number (PNO) that is used to identify Major Defense Acquisition Programs (MDAP) and Major Automated Information System (MAIS) Acquisition Programs. When implemented, all Acquisition Category (ACAT) level programs will be required to be registered in the APUID Registry.

The following provides an example of the program description that would be provided using the level 2 WBS for guidance:

- | Level 1 | Level 2 |
|---|---|
| <ul style="list-style-type: none">• DoD Aircraft Program XX | <ul style="list-style-type: none">• Air Vehicle (AV)• Systems Engineering/Program Management• System Test and Evaluation• Training• Peculiar Support Equipment• Common Support Equipment• Operational/Site Activation• Industrial Facilities• Initial Spares and Repair Parts |

Detailed guidance on the work breakdown structures for defense materiel items is located at http://www.acq.osd.mil/pm/currentpolicy/wbs/MIL_HDBK-881A/MILHDBK881A/WebHelp3/MILHDBK881A.htm

Business/Financial Management Analysts: Prior to providing Contracting Office officials with requests for procurement of services or material, business/financial management analysts must insure that requested items or deliverables are distinguished by accounting treatment (e.g. operating materials and supplies; inventory; military equipment; internal-use software; other general property, plant, and equipment; expenses; etc.). These requests are usually associated with the Procurement Requests, Purchase Requisitions, Military Interdepartmental Purchase Requests (MIPRs) or similar documents when an item is requested to be procured or purchased. Each type of deliverable must be uniquely distinguishable and identified individually as a separate line item on the requisition.

Proper Financial Accounting Treatment for Military Equipment Valuation

The business/financial management analysts will work with the Program Manager to ensure that the program structure facilitates the determination of the proper financial accounting treatment. The following provides an example of program structure and the corresponding financial accounting treatment.

- Air Vehicle (AV)
 - Capitalize as - Military Equipment (if greater than \$100,000)
 - Expense (if less than \$100,000)
- Systems Engineering/Program Management - Expense
- System Test and Evaluation - Expense
- Training - Expense
- Data - Expense
- Peculiar Support
 - Capitalize as – General Property and Equipment (if greater than \$100,000)
 - Expense (if less than \$100,000)
- Common Support Equipment
 - Capitalize as – General Property and Equipment (if greater than \$100,000)
 - Expense (if less than \$100,000)
- Operational/Site Activation - Expense
- Industrial Facilities – Capitalize as – Real Property (if greater than \$100,000)
 - Expense (if less than \$100,000)
- Initial Spares and Repair Parts – Asset – Inventory

Detailed guidance on accounting policy and procedures may be found in the DoD Financial Management Regulation (FMR) Volume 4 located at <http://www.dod.mil/comptroller/fmr/04/index.html> and on the military equipment website located at <http://www.acq.osd.mil/me/index.htm>.

Contracting and Procurement Personnel: This initiative does require contracting and procurement personnel to have detailed knowledge of accounting policy or to determine the proper asset classification of such items on the DoD financial statements. Business financial management analysts, who support the accounting transactions for the program, will identify to the contracting officer the items and services to be acquired, segregated by accounting treatment within the requests for procurement of services or material. Segregating these items by accounting classification will ensure that the proper contract line item (CLIN) or subline item (SLIN) will be created to reflect the distinction necessary to facilitate appropriate financial accounting treatment. DoD regulations regarding CLIN/SLIN structure are set forth in DFARS 204.7103 and 204.7104.

Based on the input received from the business financial management analysts, contracting officers shall structure proposals, solicitations, contracts, and/or orders determined to be for or related to the acquisition of military equipment so that each type

Proper Financial Accounting Treatment for Military Equipment Valuation

of item or service is properly segregated. This structure will be used by the contracting officer to ensure that a separate contract line item (CLIN) or subline item (SLIN) structure will be created to reflect the distinctions necessary to facilitate appropriate final accounting treatment. The CLIN and SLIN structure shall be in accordance with DFARS 204.7103 and 204.7104. These DFARS provisions are located at http://www.acq.osd.mil/dpap/dars/dfars/html/current/204_71.htm.

**Proper Financial Accounting Treatment for Military Equipment Policy Implementation
SELF-ASSESSMENT QUESTIONNAIRE**

1. Implementation.
 - a. Identify policy or implementing guidance that you have already published or plan to publish.
 - b. Identify process improvements or changes that you currently have in place or plan to put into place.
 - c. Identify other policy or processes that are barriers to implementing this policy, as well as any recommended or planned corrective actions.
 - d. Provide recommendation, with rationale, for any new Department-wide implementing guidance or policy that you believe is needed to achieve full compliance with this policy.
2. Business Process or System Changes.
 - a. Identify any business system changes that you have already implemented or plan to implement.
 - b. Identify business system capabilities that are barriers to implementing this policy, and any recommended or planned corrective actions.
3. Training.
 - a. Identify training that you have already implemented or plan to implement.
 - b. Identify training limitations that are barriers to implementing this policy, as well as any recommended or planned corrective actions.
 - c. Provide recommendation, with rationale, for any new training or tools that you believe are needed Department-wide to achieve full compliance with this policy.
4. Outreach and Communication.
 - a. Identify outreach and communication activities that you have already conducted or plan to conduct to implement this policy.
 - b. Provide recommendation, with rationale, for any additional Department-wide outreach and communication activities that you believe are needed to achieve full compliance with this policy.
5. Measures of Effectiveness: Provide the proposed measures of effectiveness to monitor implementation of this policy.
 - a. Metric Description
 - b. Metric Formula.