



Defense Commissary Agency Annual Financial Report

Fiscal Year 2018

TABLE OF CONTENTS

Foreword	2
Director's Message	4
DeCA-At-A-Glance	7
The DeCA Mission, Values, Vision, Goals	8
Part I Management's Discussion and Analysis	12
Overview of DeCA	13
Organization and Mission	13
2018 Highlights	15
Sources of Funds	16
Strategic Plan and Performance Measures	16
Introduction	16
Strategic Planning	17
Aligning Planning and Performance	18
Financial Statement Summary	19
Controls and Statement of Financial Assurance	23
Limitations of the Financial Statements	26
Part II Planning and Performance Section	28
Performance Management - Balance Scorecard Results	29
Governance and Accountability	35
Continuous Process Improvement	36
Innovation	36
Summary	36
Part III Financial Section	38
Message from the Chief Financial Officer	39
Financial Statements	41
Notes to the Financial Statements	45
Required Supplementary Information	60
Independent Auditors' Report	64
Exhibit A – Material Weakness	69
Exhibit B – Noncompliance	71
Exhibit C – Status of Prior Year Findings	74
Exhibit D - Management's Response to Auditors' Report	75
Glossary of Acronyms	78

FOREWORD

The Defense Commissary Agency (DeCA) is a reporting entity of the Department of Defense (DoD). The Office of Management and Budget (OMB), which implements the Chief Financial Officers (CFO) Act of 1990, accordingly requires the DoD to use DeCA's financial statement information to prepare the annual DoD financial statements.

Under the CFO Act, OMB also requires DoD and other agencies to incorporate their annual financial statements into a Performance and Accountability Report (PAR) or an alternative Agency Financial Report (AFR). Although DeCA is not required to prepare a separate PAR or AFR, this document, which is aligned to the statutory guidance framework, has been prepared to enhance the presentation of performance, management, financial information, and to demonstrate a higher standard of accountability. DeCA will post its FY 2018 Annual Financial Report at www.commissaries.com by the end of the 1st Quarter, FY 2019.



This page intentionally left blank

DIRECTOR'S MESSAGE

New and ongoing initiatives highlighted a busy fiscal year 2018 for the Defense Commissary Agency. The agency continued to deliver the benefit to military communities during crisis events such as Hurricane Lane in Hawaii, Hurricane Florence on the East Coast and Typhoon Trami in Okinawa. The year also saw DeCA continuing the deployment of its Enterprise Business Solution (EBS) and launching new programs that enhanced the value of the commissary benefit for millions of our authorized patrons worldwide.

Here are just some of the agency's accomplishments during the fiscal year:

- **Commissary Store Brands.** DeCA originally launched three lines for the agency's private label brands: HomeBase, for nonfood items, Freedom's Choice for food items, and TopCare health and beauty items. DeCA has since launched two more lines: Tippy Toes for baby items and Full Circle Market for organic foods. Cumulative sales total more than \$70 million. Included in DeCA's assortment of more than 700 items are salad dressing, canned vegetables, plastic trash bags, honey and many more popular items
- **Enterprise Business Solution.** The agency continued developing and implementing its Enterprise Business Solution (EBS). EBS is a fully integrated solution that will modernize our resale business operations including all processes associated with a vendor and supplier portal: contracting, cataloging, pricing, promotions, planogramming, ordering, receiving and inventory, customer relations management, point-of-sale with electronic and mobile commerce, financial management and warehouse management. The year marked deployment of Increment 1 capabilities highlighted by Relex, an integrated store-specific planogramming application, and Bill Back Manager, the replacement of DeCA's AVCM (automated vendor credit memo) process. This year's deployments also included Increment 2 Capabilities: Power DAX and Power IM (Inventory Management). Under development are Increment 3 Capabilities: POS (Point of Sale) and CRM (Customer Relations Module) to be deployed in early FY 2019, and Increment 4 Capabilities: FIM (Financial Information Module) and WMS (Warehouse Management System) to be deployed in late FY 2019.
- **Your Everyday Savings! (YES!).** June 1, the marketing directorate launched the first wave of YES! items, which now total about 565 line items, to all CONUS locations. The second wave of items, launched Oct. 1, contained approximately 365 additional items. Plans are being developed to expand the program to the Alaska and Hawaii markets in the near future.
- **Natural Disasters.** This year the commissary system again weathered its share of damaging storms such as Typhoon Trami in Okinawa, Japan; Hurricane Florence on the East Coast and Hurricane Lane in Hawaii.
- **NEXCOM GIFT CARD.** The sale of DeCA gift cards are on the rise with the expansion of store distribution at Navy Exchange Command (NEXCOM) retailers. The first DeCA

gift cards were sold at Naval Air Station Oceana's Navy Exchange in Virginia beginning May 18. DeCA gift cards sold at NEXCOM retailers provide an open value option of \$5 - \$300, while current DeCA gift cards are sold in commissaries at \$25 - \$50 increments. The open value card availability will be phased in as the new point of sale system is deployed in commissary stores. At the end of FY18, Navy Exchange retailers had sold over 271 DeCA gift cards totaling more than \$27,000.

In early FY19 DeCA will expand into selling NEXCOM gift cards at 47 select Navy commissaries around the world. Navy Exchange gift cards can only be redeemed at military exchange locations, not at DeCA commissaries.

- **Exchange joint promotions.** DeCA collaborated with our exchange partners on the following promotions; Month of the Military Child, Healthy Lifestyle Festival and Back-to-School. In addition, the agency conducted joint, bounce-back coupon promotions with the Navy Exchange for Christmas, Memorial Day, Fourth of July and Labor Day plus a joint promotion centered around Father's Day.
- **Military Star Card.** Commissaries began accepting the Military Star Card on Oct. 3, 2017, being used in over 2.8 million transactions worldwide during FY18, with sales of \$202.5 million. In addition, DeCA has earned over \$2 million in revenue share income. The average Military Star Card user also spent about 20 percent more on each visit to their commissary.
- **Grand opening.** Camp Humphreys, South Korea, opened Feb. 7 as the largest commissary in the Pacific theater offering customers more options than before. The new state-of-the-art store cost a little over \$16 million to build and features 124 skylights and freezer and chill cases with energy efficient lights. On opening day, the store served more than 2,300 patrons and did over \$141 million in sales. The grand opening was a huge success and the store is considered a showcase in the Far East and is a great reflection on the hard work of Team DeCA.
- **Modified Audit Opinion.** DeCA is in its 17th year of being audited by an external auditing firm. Based on changes to our business model and other inventory transformation efforts, our FY2018 financial statements received a modified opinion. DeCA will continue its long history of being good stewards of the taxpayers' dollars. Our dedicated financial teams, stringent internal controls, comprehensive reconciliations and our partnership with DFAS have each played a role in the sustainment of our financial accomplishments.
- **Scholarships for Military Children.** Administered by the Fisher House Foundation, the program awards scholarships to eligible military children. This year, 700 students from military families received a \$2,000 scholarship courtesy of the Scholarships for Military Children program. In the past 18 years over \$18.1 million have been awarded to 10,814 recipients.

- **Planogram Reset.** The planogram and reset team performed resets in 18 stores in 2018. Utilizing a combination of partial and full shelving replacements required each store to go through a total reset, allowing the store to update and adjust the categories in the store’s shopping flow. It took months of planning and communication between the team and store to empty all the shelves, reset them, and restock the entire store. It was an ambitious schedule and completing each store with just one business day’s closure is a great example of store and HQ teamwork.
- **Commissary Rewards Card.** Since the 2012 launch of the Commissary Rewards Card, patrons have enjoyed access to digital coupons worth millions of dollars, saving them even more on their groceries. Through the end of September, over 1.1 million cards have been registered and our patrons have saved almost \$15 million, while redeeming nearly 13 million coupons.
- **DeCA’s Online Presence.** DeCA is using social media platforms as another avenue for reaching out to our patrons. The Agency is active on the following social media platforms:
 - YouTube: 215 videos on the site, 210,005 total views, and 699 subscribers
 - Facebook: 62,869 followers
 - Twitter: 5,630 followers
 - Pinterest: 844 followers
 - Instagram: 800 followers

No matter the challenge or location, DeCA is working hard to provide the best possible benefit for our servicemen and women and their families. Not even hurricanes could stop the Agency from delivering the benefit. In those times Team DeCA pulled together – often in spite of their own losses – to help keep the commissary benefit flowing to our men and women in uniform and their families.

BIANCHI.ROBERT.
JOHN.1028082378

Digitally signed by
BIANCHI.ROBERT.JOHN.10280
82378
Date: 2019.01.18 11:40:34 -05'00'

Robert J. Bianchi
By direction

DECA-AT-A-GLANCE

Established as a Provisional Organization:	May 15, 1990
Formally Established:	Nov. 9, 1990
Officially Activated:	Oct. 1, 1991
Headquarters:	1300 E Avenue, Fort Lee VA 23801-1800 www.commissaries.com www.facebook.com/YourCommissary www.twitter.com/TheCommissary www.youtube.com/DefenseCommissary
Fiscal 2018 sales:	\$ 4.7 billion
Fiscal 2018 total revenue:	\$ 5.0 billion
Fiscal 2018 operations cost:	\$ 1.3 billion
Total employees:	13,000 +
Total authorized households:	Approximately 5.4 million
Customer transactions:	83 million
Global presence:	13 countries, 2 U.S. territories
Commissaries as of 30 Sep 2018:	237

DeCA MISSION

Deliver a vital benefit of the military pay system that sells grocery items at cost while enhancing quality of life and readiness.



DeCA VISION

Understand our Customers and Deliver a 21st Century
Commissary Benefit

DeCA VALUES

We have **PASSION** for what we do!

- **P: We Pursue** excellence
We pursue excellence and are motivated to be the best we can be every day. We work together integrating our values, moving toward one vision. We go the extra mile to satisfy our customers, both internal and external.
- **A: We are Accountable** and fiscally responsible
We are accountable and fiscally responsible, which is shown through our daily actions as we perform our jobs. We are accountable for the results of our actions. We work together in a collaborative fashion and treat our customers (internal and external), fellow coworkers, and stakeholders with integrity, respect, and honesty. We make the right decisions and are held accountable for them, keeping our values in mind when making them.
- **S: We have a Sense** of urgency
We have a sense of urgency to quickly and efficiently accomplish the expectations of those who rely on us. In critical times we are responsive by providing support for those who need it most. This urgency extends to providing a taste of home and a sense of community to deployed military members and their families.
- **S: We set high Standards**
We are committed to setting high standards at all levels within the organization, ensuring we excel in our ultimate goal – providing our patrons outstanding customer service, quality products at great prices, and an excellent atmosphere in which to shop. We work collaboratively in all areas of the organization to make this happen.
- **I: We value Innovation**
We encourage innovation in order to progress the Agency towards greater efficiencies and effectiveness. We promote collaboration to initiate change that allows us to do our jobs more proficiently. We maintain the mindset that we can always do better and look for ways to make that happen.
- **O: We take Ownership** of our performance
We take ownership of our performance by knowing what our expectations are and setting targets to exceed them. We, as individuals, ensure what we do on a daily basis supports and aligns with the Agency mission.
- **N: We are Necessary**
We are necessary to the well-being and quality of life of our military families. We provide a tangible value through the benefit of savings, which benefits our patrons financially. We also provide a community value through the various community support endeavors... scholarships, spousal employment, exchange partnerships with family fitness festivals, and others. A sense of community is critical during the stressful times of spousal deployment and unfamiliar settings. We are the link in supporting our patrons for products and services that are familiar, valued, and represent their choices.

One Vision, One Team, One DeCA!

DeCA GOALS

1 - Provide service members and their families with a quality benefit at significant savings.

2 - Sustain a capable, diverse and engaged civilian workforce.

3 - Be a model organization through agility and governance.



This page intentionally left blank

PART I

MANAGEMENT'S DISCUSSION AND ANALYSIS



OVERVIEW OF DeCA

ORGANIZATION AND MISSION:

The Defense Commissary Agency (DeCA or the Agency) is a component of the 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. In order to provide better service to military patrons at a lower cost, the Commission recommended consolidation of the four separate commissary systems, which established DeCA on October 1, 1991.

DeCA is headquartered at Fort Lee, Virginia and operates a worldwide system of 237 commissaries. Our commissaries sell food and related household items to active, Reserve, and Guard members of the Uniformed Services, retirees of these services, authorized family members, and other authorized patrons.

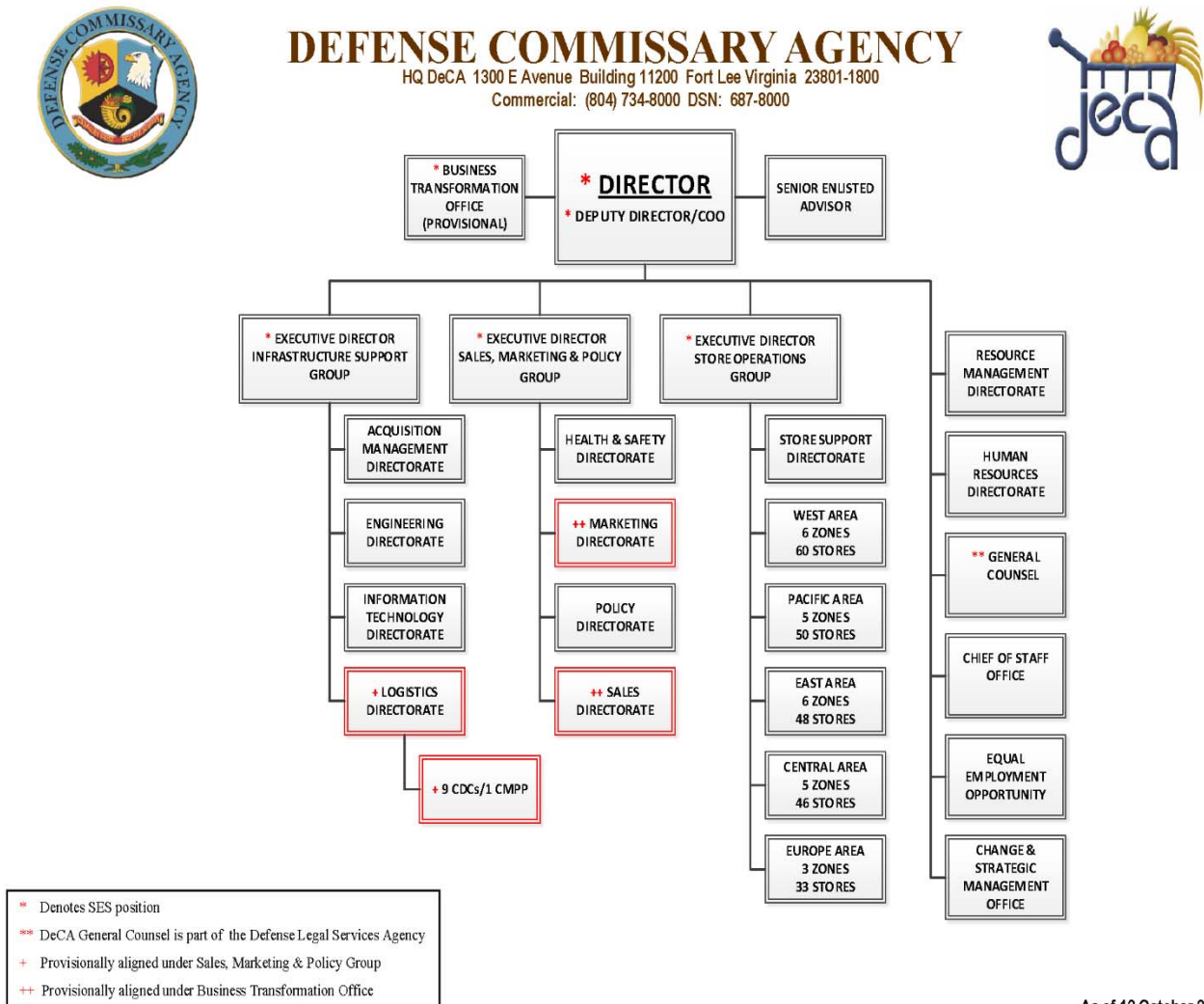


Five area offices provide localized management and support for the agency's commissaries. Three of these offices, East, Central, and West, manage stores in the continental United States (US)

and Puerto Rico. The other two area offices, Europe and the Pacific, manage stores in Europe, Africa, and Asia. Within the operational areas, zone managers are responsible for 9 to 10 stores. Zone managers and assigned store directors jointly provide leadership and direction for their stores, building positive customer service in each commissary.

DeCA also operates central distribution centers (CDCs) in Europe and the Pacific. Field operating activities perform services for area operating elements and their commissaries, including centralized purchasing of national-brand sales items.

The organizational structure of DeCA for fiscal year (FY) 2018 is shown in the following chart:



As of 12 October 2017

2018 HIGHLIGHTS:

During FY 2018, DeCA's operations included commissaries with annual sales of approximately \$5.0 billion and approximately 83 million customer transactions. DeCA operates its commissaries around the world to support the military services. Patrons include Active, Reserve, and Guard members of the Uniformed Services, retirees of these services, authorized family members, DoD civilian employees overseas, and other authorized categories. Congress authorizes DoD to operate its commissaries as a significant nonpay benefit to supplement military income as an integral part of the overall military pay and benefit package. DeCA sells its groceries and household supplies to the military community at its approximate cost. There is a one percent added that was originally to cover loss incurred in normal operations. This cost plus one percent historically represented our shelf price which was the basis for inventory valuation plus the count of product behind the shelf label, regardless of SKU. DeCA is now able to variable price products for resale in order to be competitive with commercial grocery enterprises while providing greater patron savings. The one percent is relevant to fully capture loss and stabilize inventory book values as we transition to a perpetual SKU based inventory that is based on latest acquisition cost. Upon full implementation and optimization of the EBS system DeCA will start utilizing a weighted average calculation within the inventory management system to comply with commercially based GAAP rules for grocery enterprises. In addition, a five percent surcharge is applied to patron purchases to finance equipment and construction projects and store equipment, including information management systems.

DeCA continues to maintain its audit readiness through continual improvements in the quality, accuracy, timeliness, and reliability of the financial information that is used to manage the Agency. Controls were consistently applied across a range of business processes to protect data quality and integrity, and to maintain a compliant audit trail within those processes. For each business process, controls were applied at the transaction level with data flowing from source documents to general ledger postings. Controls were also in place to produce accurate trial balances for proper period closeouts, which, in turn, allowed the preparation of financial statements that auditors could cost-effectively review and verify. In FY 2018, DeCA continued its role as a leader in the DoD's compliance with OMB Circular No. A-123, "*Management's Responsibility for Enterprise Risk Management and Internal Control*" and Appendix A: "*Internal Control over Financial Reporting (ICOFR)*." The foundation for that program is the ongoing assessment of risk and mitigating controls and the subsequent development, refinement, and implementation of appropriate, cost-effective controls. DeCA's leadership is committed to maintaining a robust environment for strong internal controls and safeguarding the resources entrusted to the Agency.

DeCA continues to maintain a program of strong financial and operational controls. In FY 2018, DeCA's Statement of Assurance reported on financial and nonfinancial operations, and financial system compliance. DeCA's Director was able to provide an unmodified statement of reasonable assurance that DeCA's internal controls met the objectives of the Federal Managers' Financial Integrity Act (FMFIA) and a modified statement of reasonable assurance for Federal Financial Management Improvement Act (FFMIA). Only the continued use of legacy financial systems, which are nonintegrated and unable to produce transactions using the United States Standard General Ledger (USSGL) prevented the Director from providing an unmodified assurance statement for the FFMIA.

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 reflect the revenues from the sale of products by the commissary stores. Products offered include groceries, meat, produce, dairy, health and beauty aids, household products, and pet supplies.

Commissary Operations finances the operating costs of commissaries, areas, and headquarters activities. The primary revenue source for this activity group is a direct appropriation to the Defense WCF, which in turn, is apportioned to the DeCA WCF. Specific costs include civilian and military labor, service contracts, travel, transportation of commissary goods overseas, and other indirect support. DeCA received approximately \$1.4 billion in appropriation transfers during FY 2018. 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, which is part of the General Fund, is primarily funded from the five percent surcharge applied to patron sales at the checkout counter. The Surcharge Collections Trust Fund resources are used for store information technology, maintenance and equipment, and the commissary construction program. The Fund does not receive appropriated fund support.

STRATEGIC PLAN AND PERFORMANCE MEASURES

INTRODUCTION:

DeCA develops and structures its planning and performance process using the framework provided in the Government Performance and Results Modernization Act (GPRAMA) (Public Law 111-352) and the associated guidance in OMB Circular No. A-11, Part 6.

The DeCA Strategic Framework is a cyclical, never ending process where one activity feeds the next allowing for continuous feedback and adjustments throughout. Our strategic planning process incorporates multiple planning tools such as a Balanced Score Card (BSC) and Strength, Weakness, Opportunities, and Threats (SWOT) analysis. We conduct quarterly data calls and metric reviews for performance management that includes an ongoing assessment of results of specific measures aligning to strategic goals and objectives. Our governance process links planning, performance, accountability and budgeting to performance management, while prioritizing investments.

DeCA's Strategic Plan lays out the roadmap for the Agency's mission and vision for the future. We strive to fulfill our mission to **"Deliver a vital benefit of the military pay system that sells grocery items at significant savings while enhancing quality of life and readiness."** The commissary benefit supports Service members and their families by providing a safe grocery shopping environment

with significant savings compared to civilian supermarkets. This mission serves as the driving force behind our goals found in the Director’s 2018 Strategic Guidance as listed below.

- **Our Customers:** Deliver a premier customer experience in every store by providing a relevant and vital benefit.
- **Our Business:** Advance our business model through the transparent management of resources and revenue.
- **Our Workforce:** Empower a capable, engaged and responsible workforce.
- **Our Culture:** Foster a culture of collaboration and change acceptance through proactive communication and inclusion.

These goals drive us towards continuous improvement in pursuit of our vision which sets forth a focus to remain relevant to our customers and enable customer service consistent with today's shopping trends. Our vision is to **“Understand Our Customers and Deliver a 21st Century Commissary Benefit.”**

STRATEGIC PLANNING:

The Agency’s senior executives maintain a strategic thinking process that considers impacts to DeCA in the near and long term. They have determined the Agency’s direction based on NDAA and DoD direction, an assessment of significant impacts, ongoing collaboration, discussions, and analysis. The Agency’s goals are achievements that reflect the top performance improvement priorities of leadership. Our strategic goals are reevaluated annually to ensure they remain relevant to our environment, stay consistent with Agency mission, and continue to support the DoD strategic priorities. Each strategic goal has supporting objectives with performance measures to track progress of success toward the desired end state.

DeCA continues to refine efforts to gain shopper insights and be sensitive to the expectations of our patrons. We are investigating the rapidly changing technology that is becoming a significant part of how patrons shop and communicate. Concepts are being evaluated and tested as we partner with the 21st century shopper.

Modernizing DeCA’s business systems and retail processes is a continuous process. This modernization is taking place in defined increments over time and will eliminate redundant and costly legacy systems, improve our business performance and incorporate commercial best practices. This transition is critical to the Agency’s future to ensure important capabilities such as customer relationship management, multi-channel retailing and marketing, enhanced e-commerce, inventory optimization, data accuracy, and analytics are available to ensure ongoing relevancy.

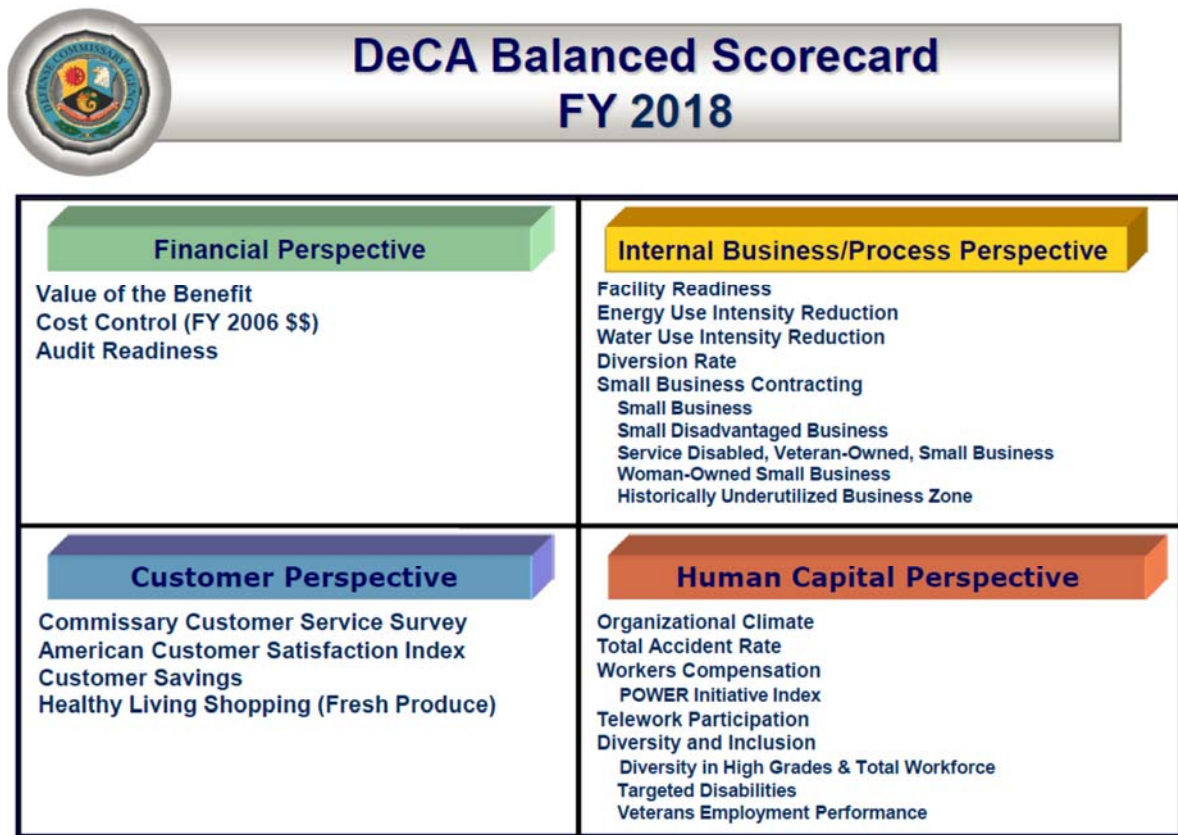
In today’s uncertain fiscal environment the Agency continues to carefully govern how resources are expended. The governance process, described further in this section, addresses how funding decisions are made. As the cost of doing business increases, there may be a need to realign,

adjust or divest to become more efficient and appropriately resource the priorities. The formal governance process ensures transparency and a structured method of determining how funds are expended. The Agency’s quarterly performance reviews and other forums ensure further analysis of investments and their data-based results to support subsequent decision-making.

ALIGNING PLANNING AND PERFORMANCE:

DeCA’s Strategic Plan communicates the Agency’s overarching direction, while linking to the Balanced Scorecard (BSC) to establish performance measures used to assess our progress. The FY18 BSC incorporates performance measures and targets across four perspectives to manage Agency performance from a holistic viewpoint. These perspectives address Agency performance in the areas of financial, customer, internal business processes, and human capital. The results of the BSC are monitored and assessed quarterly to enable data based decision-making. The quarterly reviews allow for executive and senior leadership collaborative discussions, transparency of activities, and opportunities for course adjustments and improved outcomes.

The following chart displays the FY18 BSC four perspectives and their associated elements:



FINANCIAL STATEMENT SUMMARY

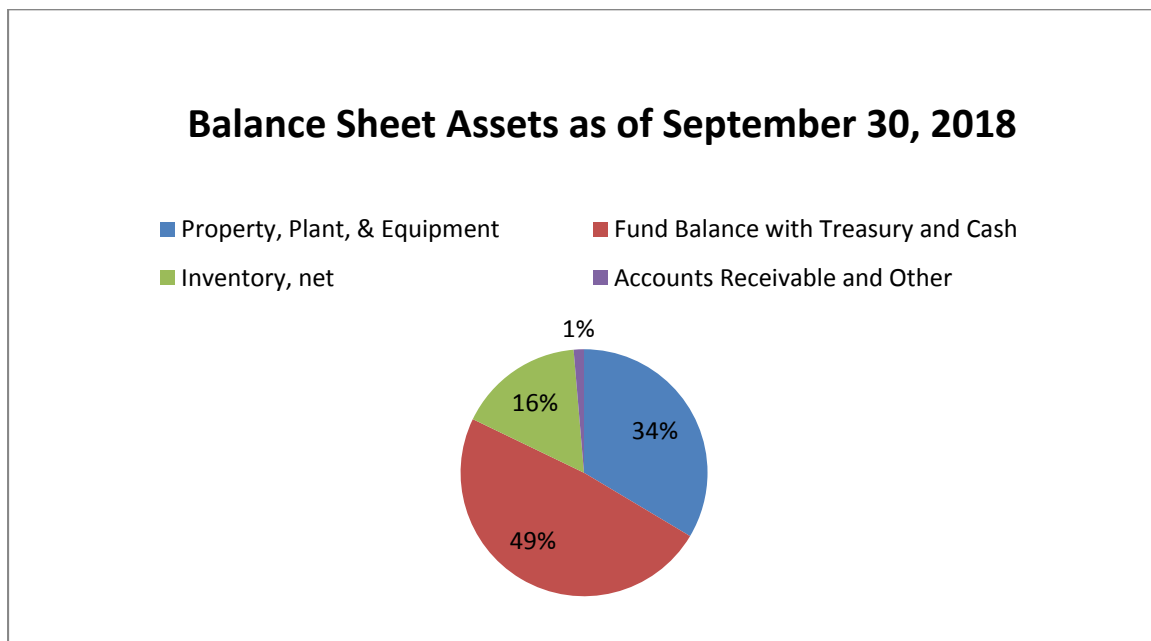
DeCA’s Consolidated Balance Sheet, Statements of Net Cost, Changes in Net Position, and Combined Statements of Budgetary Resources (consolidated financial statements) have been prepared to report the financial position and results of operations for the entity, pursuant to the requirements of Title 31, United States Code (U.S.C.) 3515 (b). These consolidated financial statements have been prepared from DeCA’s books and records in accordance with the formats prescribed by the OMB. These consolidated financial 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 consolidated financial 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 financial statements are presented in a two-year comparative format. The following section provides a brief description of each consolidated financial statement along with relevant information that will aid the reader in understanding the financial components of DeCA.

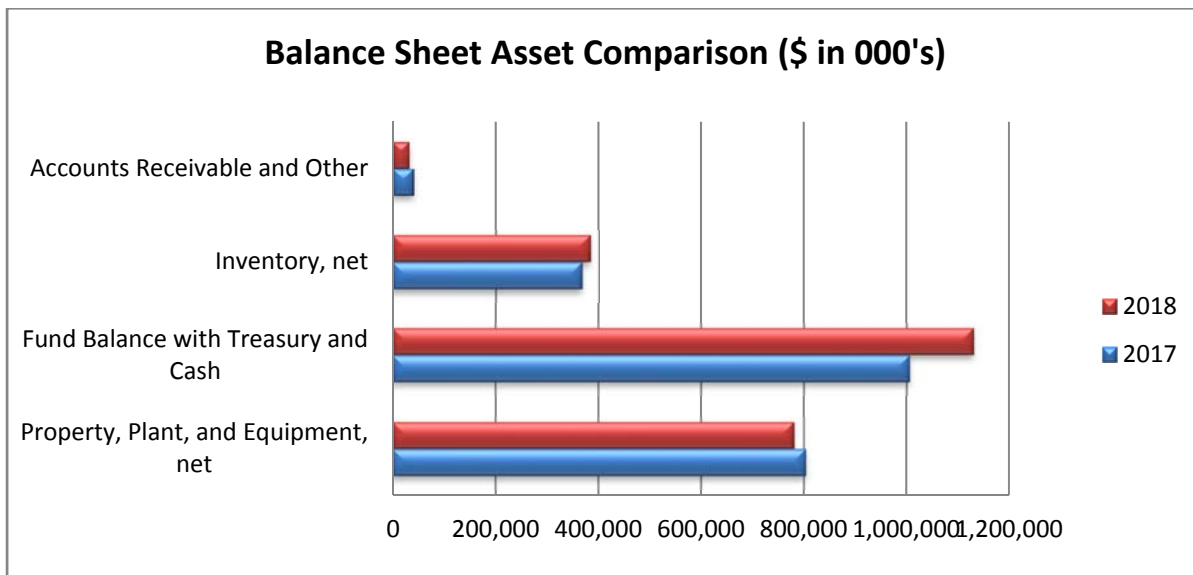
CONSOLIDATED BALANCE SHEETS:

The consolidated 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 – On September 30, 2018, DeCA reported assets of \$2.3 billion. Assets are the resources available to pay liabilities or satisfy future service needs of the Agency. 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, 2018 and September 30, 2017, along with discussions of significant fluctuations.



Accounts Receivable and Other comprises 1 percent of DeCA’s current year assets. These represent amounts primarily due from DeCA customers. Accounts receivable and other remained relatively consistent when compared to prior year balances.

Inventory, net represents 16 percent of DeCA’s current year assets and is comprised of grocery, meat, and produce items held for resale to DeCA patrons. Inventory remained relatively consistent when compared to prior year balances.

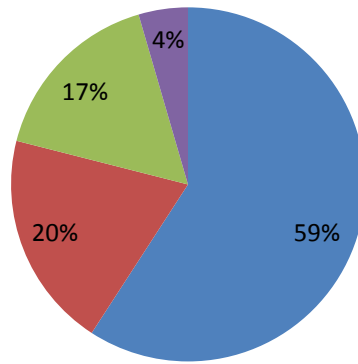
Fund Balance with Treasury (FBWT) and Cash represents 49 percent of DeCA’s current year assets. Funding is primarily made available through the U.S. Department of the Treasury accounts from which DeCA makes expenditures to pay liabilities. FBWT also includes monies generated from sales at commissaries that have been deposited to an authorized financial institution. Cash consist of deposits that have been deposited in the authorized financial institution, but not processed and sales that were not recorded in the accountable period due to end of month cutoffs in the accounting system. FBWT and Cash remained relatively consistent when compared to prior year balances.

General Property, Plant, and Equipment (PP&E), net represents 34 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 remained relatively consistent when compared to prior year balances.

Liabilities – On September 30, 2018, DeCA reported liabilities of \$664.8 million. Liabilities are probable and measurable future outflows of resources arising from past transactions or events. The following chart displays DeCA’s major categories of liabilities as a percentage of total liabilities.

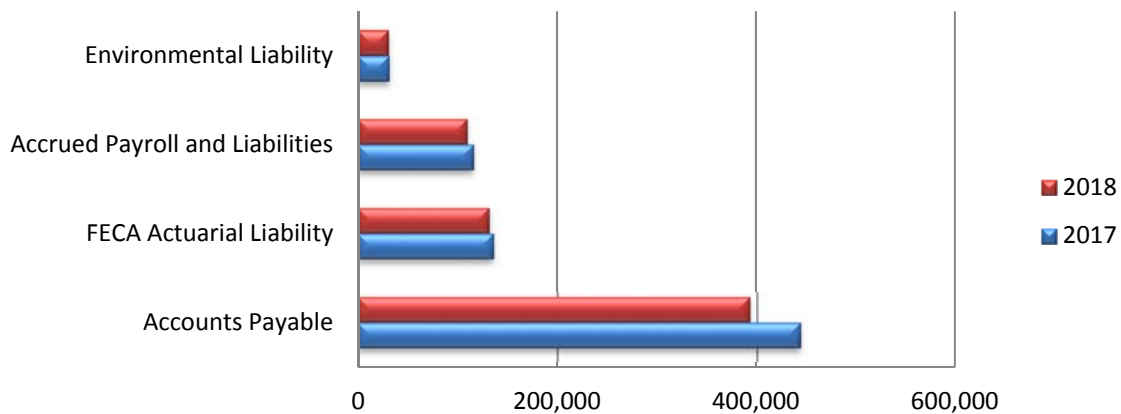
Balance Sheet Liabilities as of September 30, 2018

■ Accounts Payable ■ FECA Actuarial Liability
■ Accrued Payroll and Liabilities ■ Environmental Liabilities



The following chart presents comparative data of major liability balances as of September 30, 2018 and September 30, 2017, along with a discussion of fluctuations.

Balance Sheet Liability Comparison (\$ in 000's)



Environmental Liabilities comprises 4 percent of DeCA's current year liabilities and are estimated costs to clean up items such as asbestos, lead paint, and other hazardous materials from our commissaries. Environmental liabilities remained relatively consistent when compared to prior year balances.

Accrued Payroll and Liabilities comprises 17 percent of DeCA’s current year liabilities and includes liabilities for accrued payroll and benefits, foreign national separation pay, and accrued leave. Accrued payroll and liabilities remained relatively consistent when compared to prior year balances.

Federal Employees Compensation Act (FECA) Actuarial Liability comprises 20 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 as well as a component for incurred, but not reported claims. The Department of Labor (DOL) calculates the liability for the DoD, who in turn allocates a proportionate amount to DeCA based upon actual workers’ compensation payments to DeCA employees over the preceding three years. The actuarial liability remained relatively consistent when compared to prior year balances.

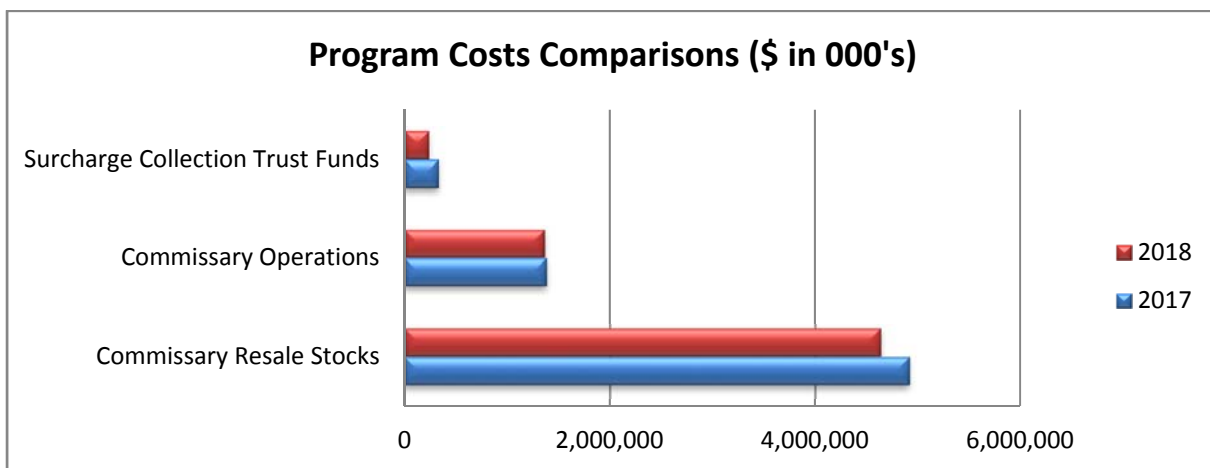
Accounts Payable comprises 59 percent of DeCA’s current year liabilities, and consists of DeCA’s liability for goods and services delivered or received, but not paid prior to year-end. Accounts payable remained relatively consistent when compared to prior year balances.

STATEMENTS OF NET COST:

The consolidated Statement of Net Cost represents 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 and to purchase and maintain computer systems and equipment at the store level;
- *Commissary Operations* includes the associated payroll and operational costs necessary to operate the commissary system; and
- *Commissary Resale Stocks* includes the costs to purchase resale inventory.

The chart below compares the gross costs between the three major DeCA activity groups.



STATEMENTS OF CHANGES IN NET POSITION:

The consolidated Statements of Changes in Net Position represents those accounting transactions that caused the net position of the consolidated 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 paid by other Federal Agencies. DeCA's net cost of operations serves to reduce net position. DeCA's net position increased by \$171.2 million, 11 percent, primarily attributable to increase in Unexpended Appropriations.

STATEMENTS OF BUDGETARY RESOURCES:

This statement provides information on the budgetary resources available to DeCA for fiscal years 2018 and 2017 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 remained relatively consistent when compared to prior year balances.

CONTROLS AND STATEMENT OF FINANCIAL ASSURANCE

OMB CIRCULAR A-123, MANAGEMENT'S RESPONSIBILITY FOR INTERNAL CONTROL OVER FINANCIAL REPORTING, APPENDIX A:

OMB Circular A-123, Appendix A is fully implemented throughout DeCA. For the past eleven years, all processes material to the financial statements have been documented and tested. In FY 2018, 238 key controls were evaluated and assessed for effectiveness. Of those key controls, 89 percent were found to be operating effectively; and 7 percent were operating adequately. The remaining 4 percent of the controls were ineffective; and although their impact is not material to the financial reports, these controls are currently undergoing corrective action plans to bring them to the required level of effectiveness. In addition to the 238 key controls there were 153 Complimentary User Entity Controls (CUECs) tested this year. The results found 153 operating effectively. There were none found to be ineffective.

The Internal Control Senior Assessment Team (SAT) also monitors the control assessments. The SAT found that both the quarterly control assessments and the financial process improvements continue to reduce annual findings by the external auditors. It also monitored the progress of the ineffective controls through formal corrective action plans, reported quarterly. All of these practices have produced more efficient operations and increased savings for the Agency.



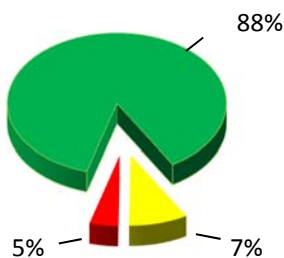
Internal Controls Over Financial Reporting



FY 2016

Testing Results:

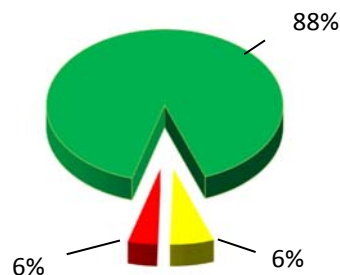
- 237 Tests Performed
- 208 Effective (88%)
- 16 w/Exceptions (7%)
- 13 Ineffective (5%)



FY 2017

Testing Results:

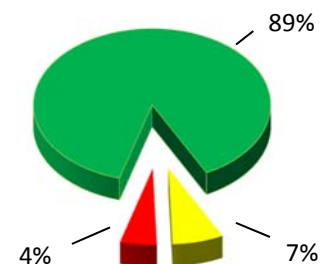
- 238 Tests Performed
- 209 Effective (88%)
- 14 w/Exceptions (6%)
- 15 Ineffective (6%)



FY 2018

Testing Results:

- 238 Tests Performed
- 212 Effective (89%)
- 17 w/Exceptions (7%)
- 9 Ineffective (4%)



Since the onset of the program, DeCA has provided timely submissions through the Office of the Assistant Secretary of Defense, Manpower & Reserve Affairs (OASD (M&RA)), to the Under Secretary of Defense (Comptroller), Financial Improvement and Audit Readiness Directorate, for the OMB Circular A-123, Appendix A Deliverables and Annual Statement of Assurance.

FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT STATEMENT OF ASSURANCE:

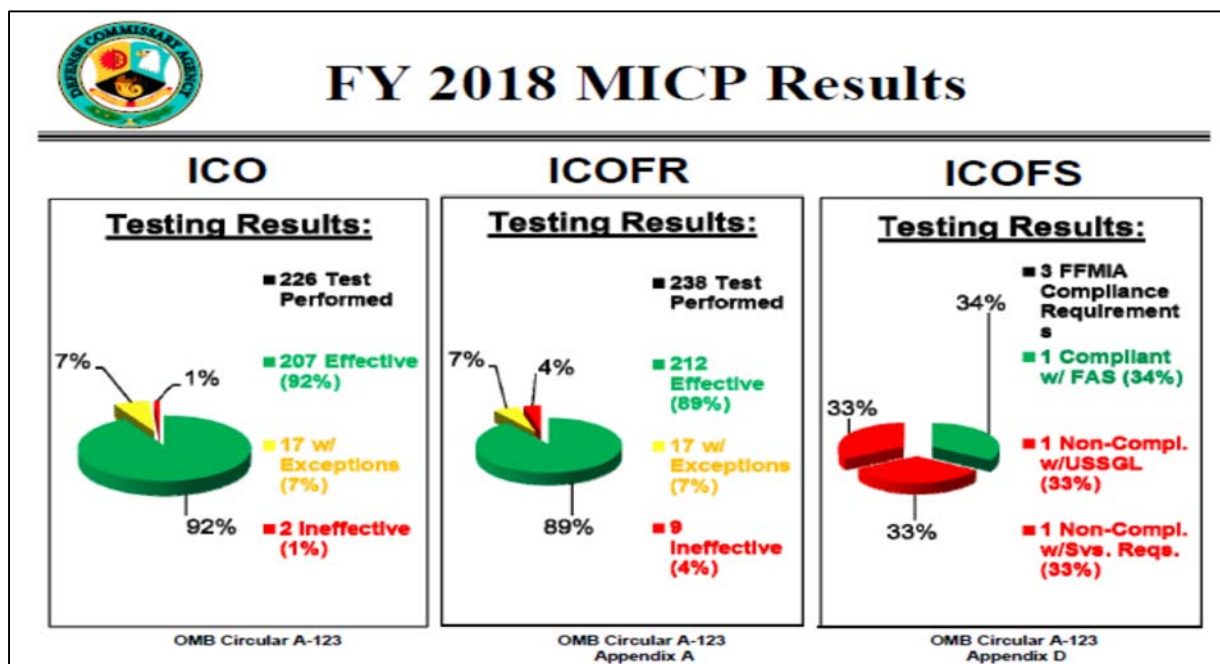
Although DeCA is not required to submit a Statement of Assurance, the DoD is required to do so; therefore, DeCA performs work to support the Department. The objectives of the system of internal accounting and administrative control of DeCA are to provide reasonable assurance that the Agency:

- Has an efficient and effective operation.
- Provides reliable financial reports.

- Complies with applicable laws and regulations.

In FY 2018, DeCA reported a Qualified Statement of Assurance related to the effectiveness of internal controls over financial reporting and operations; however DeCA’s systems do not conform to the financial management systems requirements and DeCA was not compliant with FFMIA. In making the determination, the Director considered information from various sources, such as management reviews, Inspector General and Government Accountability Office reports, the audit of the financial statements, and reviews of financial and administrative systems. The cornerstone of the FY 2018 Statement of Assurance is the Agency’s financial improvement plan where we continue to utilize the OMB Circular A-123, Appendix A methodology. Through assessments, discovery, correction and monitoring, we continue to strive for increased efficiency and effectiveness utilizing this well-established tool.

The following chart illustrates the results of the FY 2018 Manager’s Internal Controls Program (MICP). Testing results are outlined for the three areas of internal controls (1) Internal Controls over Operations (ICO); (2) Internal Controls over Financial Reporting (ICOFR); and (3) Internal Controls over Financial Systems (ICOFS).



FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT STATEMENT OF ASSURANCE:

DeCA’s legacy financial systems are not compliant with federal financial management system requirements and the USSGL at the transaction level. To meet these requirements, DeCA, jointly with the DoD, is actively working on improving the system-wide architecture in order to be fully compliant with FFMIA. DeCA continues to employ a system of processes and controls that adequately mitigate

the risks associated with this issue. Therefore, DeCA reported a Qualified Statement of Assurance for noncompliance of the FFMIA.

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 DoD to comply with the *Chief Financial Officers Act of 1990* and the *Government Management Reform Act of 1994*.

While DeCA's financial statements have been prepared from its books and records in accordance with U.S. generally accepted accounting principles, the financial 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 financial 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.

This page intentionally left blank

PART II

PLANNING AND PERFORMANCE



PERFORMANCE MANAGEMENT - BALANCED SCORECARD RESULTS

DeCA is using the BSC concept for measuring performance in meeting our strategic goals and objectives. The BSC brings together, on a single management report, key financial and nonfinancial performance measures that allow DeCA to clarify our vision and strategic objectives. DeCA's performance in the BSC's four perspectives of Financial, Internal Business/Process, Customer, and Human Capital for FY 2018 are summarized below.

FINANCIAL PERSPECTIVE

Performance Measure	FY 2018 Targets	FY 2018 Actual
Value of the Benefit	ROI \geq \$1.25 Customer Savings to \$1.00 Appropriated Costs	\$1.15
Cost Control (FY 2006 \$\$)	<\$1,203M	\$934M
Audit Readiness	Unmodified Opinion	Modified Opinion

The **Value of the Benefit** (i.e., return on investment or ROI) is expressed as the value received by the patron in commissary dollar savings for shopping and obtaining food and other merchandise at significant savings in the commissary, divided by the taxpayer dollar cost of providing the benefit. FY18 results are not available at this time.

The **Cost Control** measure is a comparison between the current and baseline annual costs using constant FY 2006 dollars. The target is that the actual costs will not exceed the FY 2006 base year costs, when adjusted to FY 2006 dollars. We met our target for FY 2018 of less than \$1,203 million, with results of \$934 million.

Audit Readiness is the ability of an organization to attest with confidence that it is ready for an independent review of its internal accounting processes, financial statements, and other nonfinancial documents, and that it has all the required documents available. Unfortunately, we fell short of our anticipated goal, with a modified opinion caused by our business transformation efforts.

INTERNAL BUSINESS/PROCESS PERSPECTIVE

Performance Measure	FY 2018 Targets	FY 2018 Actual
Facility Readiness	83.8%	84.4%
Energy Use Intensity Reduction		
<ul style="list-style-type: none"> • DoD Goal (FY 2015 Baseline: EO 13693) 	120.1 kBTU/SF/Yr	123.8
<ul style="list-style-type: none"> • DeCA Goal 	35% below retail grocery	40.4%
Water Use Intensity Reduction	14.2 Gal/SF/Yr	13.3
Diversion Rate	60%	63.3%
Small Business Contracting Goals (Assigned by DoD)		
Small Business (SB)	60.00%	68.96%
Small Disadvantaged Business (SDB)	5.00%	22.96%
Service Disabled, Veteran-Owned, Small Business (SDVOSB)	3.00%	14.34%
Woman-Owned Small Business (WOSB)	5.00%	8.67%
Historically Underutilized Business Zone (HUB Zone)	3.00%	12.77%

Facility Readiness: The Facility Readiness metric indicates the percentage of DeCA facilities with a Facility Condition Index (FCI) of 80% or higher. The FCI is a composite metric that indicates the physical condition of a facility and the impact of facility investment programs. A Government-developed software program, BUILDER, has been implemented to replace DeCA’s previously assessment methodology. In April 2014, OSD established a Facility Sustainment and Recapitalization Policy, setting the FCI goal of 80% for all DoD facilities. DeCA successfully implemented BUILDER during 2014, and established a baseline in FY 2015 of 80.8% for its facilities, with goals for the out-years set to reflect a 1% improvement each year, utilizing the FY 2015 baseline, based on available sustainment funding. The results for FY18 were 84.4%, exceeding the goal of 83.8%.

Energy Use Intensity Reduction: Energy Use Intensity (EUI) is measured as annual energy use in thousands of British Thermal Units (kBtUs) divided by gross building area in square feet (sf). DeCA has worked hard to reduce energy use since 1993 and achieved high levels of energy efficiency prior to the establishment of Federal and DoD standards. Executive Order 13693 established new energy use intensity reduction goals for all federal facilities. Displaying energy usage on a “per unit of gross floor area” basis allows comparisons between facilities of different sizes and takes into account the addition and demolition of facilities. The Executive Order calls for reducing the EUI by 2.5% per year from FY2015 to FY2025, for a total reduction of 25%. DeCA’s EUI for FY15 (the new baseline) is 129.8 kBtU/SF/year. FY 2018 results were 123.8, slightly missing the goal of 120.1. In addition to the DoD and Federal goals, DeCA has an energy use target to enable comparison to commercial grocery stores. DeCA will seek to maintain a level of energy use in commissaries at least 35% below the energy use for comparable private sector grocery stores. FY2018 results were 40.4%, exceeding our goal of 35%. The comparison uses an energy use intensity index for commercial buildings at: <http://buildingsdatabook.eren.doe.gov/CBECS.aspx>.

Water Use Intensity Reduction: Executive Order 13423, January 2007, established the Water Use Intensity (WUI) reduction goals for all Federal facilities. It called for reducing the WUI by an average two percent per year from FY 2007-2016, for a total of 18 percent. DeCA’s FY 2007 WUI baseline was 18.2. Executive Order 13514, October 2009, further extended the two percent per annum consumption reduction goal to 2020. The metric is percent reduction of Water Use Intensity (WUI) in gal/sf/yr. DeCA’s 2020 WUI goal is 13.5 gal/sf/yr. This goal was passed down from the Department of Defense to DeCA. Executive Order 13693, March 2015, further extended the 2 percent per annum consumption reduction goal to 2025. DeCA’s 2025 WUI goal is 11.6 gal/sf/yr. Prior to FY 2013, DeCA expressed its Balanced Scorecard water use reduction goal as 2% per year. For FY 2013 and beyond, DeCA is stating its goal as the cumulative percent reduction required for the target year as compared to the 2007 baseline. The FY 2018 results were 13.3 gal/sf/yr, exceeding the goal of 14.2 gal/sf/yr.

Diversion Rate: The metric refers to reducing the Agency’s volume of solid waste that is diverted from the landfill. According to DoD Guidance for EO 13693 (March 2016), the DOD goal is 50% solid waste diversion. Up until FY 2017, DeCA did not have the data available through our Waste Management Reporting system (WMR) to establish a baseline so we could measure our success for diversion. In 2017 we were only measuring the recycling efficiency of cardboard, plastic and paper. However, the Agency has, through the new system, been able to track and measure the diversion of all materials created by the Agency. One large factor in measuring our diversion is the establishment and growth of the food bank donation program which averages approximately 3 million pounds of donated food being diverted from the waste stream. The FY 2018 goal was 60% and results exceeded at 63.3%.

Small Business Contracting: Beginning in FY 2012, as required by the Department of Defense (DoD), a mandatory performance requirement that addresses small business contracting goals was added to performance plans for DeCA’s Senior Executives. In order to ensure that appropriate visibility and emphasis are placed on these requirements within DeCA, the Agency includes these goals on its Balanced Scorecard. Agency-level goals in the categories shown are established annually by the DoD Office of Small Business Programs (OSBP) based on historical small business contracting achievement by the Agency, with consideration of anticipated spends. Goals for each FY are assigned after all reporting is completed for the previous FY. DeCA’s achievement figures will represent the

total dollars awarded within the various small business categories as a percentage of the total eligible contract dollars awarded by the Agency for each FY. The Agency exceeded all targets in all categories for FY18.

CUSTOMER PERSPECTIVE

Performance Measure	FY 2018 Targets	FY 2018 Actual
Commissary Customer Service Survey (CCSS)	A	B
American Customer Satisfaction Index (ACSI)	Meet or Exceed Industry Average and DeCA prior year ACSI	Industry: 79 DeCA FY 17: 74 DeCA FY18: 71
Sustain Customer Savings	23.7%	TBD
Better for You Shopping (Fresh Produce)	9.35% (as a % of total sales)	9.55%

The **Commissary Customer Service Survey (CCSS)** is an internal DeCA survey that is conducted annually to assess patrons’ overall satisfaction with the commissary system, using tablets for electronic data entry as the survey instrument. The CCSS rating scale is from 1 to 5, with 1 being very poor and 5 being very good. We convert the numerical survey results to letter grades. To achieve a grade of “A”, a score of 4.5 or better is required. The FY 2018 score of B (4.36) did not meet our goal of scoring A.

American Customer Satisfaction Survey: The ACSI is an external survey produced annually through a partnership of the University of Michigan Business School, the American Society for Quality, and the internal consulting firm Claes Fornell International (CFI) 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 conducted November-December of each year and reported to the Agency during February of the following calendar year. The results are reported for the fiscal year. For FY 2018, DeCA updated the scoring process comparison to a two-facet measure for the ACSI. The revised measure continues to compare DeCA’s score directly to the industry average and then secondly to DeCA’s prior year score. DeCA’s FY 2018 ACSI score was 71, which is lower than the industry average of 79, and slightly lower than the DeCA FY 2017 ACSI score of 74.

Sustain Customer Savings: In accordance with requirements of the FY 2016 National Defense Authorization Act (NDAA), as modified by the FY 2017 NDAA, the Customer Savings results were rebase-lined for FY 2016 through development of a new methodology to measure patron savings which builds on DeCA’s prior approach by incorporating a market basket component of items

with local competitor comparisons of the items. The baseline of 23.7% will be used to determine savings goals for FY 2017 and beyond. FY 2018 results are not yet available; however, current data as of end of FY18(Q3) shows 24.4% savings.

Healthy Living Shopping (Fresh Produce): In support of DoD efforts to improve the health of our military members and patrons, emphasis was placed on increasing produce consumption. DeCA looked at the growth rate of the FY 2015 baseline and concluded that the growth would be unsustainable for outyear goals. DeCA, in FY 2016, reset the FY 2015 baseline to 9.05% growth in order to obtain more realistic growth goals. The FY 2018 target percent of produce sales (excluding flowers and plants) is 9.35%. For FY 2018, DeCA has exceeded its target and achieved 9.55% of produce sales as a percent of total net sales.

HUMAN CAPITAL PERSPECTIVE

Performance Measure	FY 2018 Targets	FY 2018 Actual
Organizational Climate	Increase in Survey Results in the High Impact Dimensions (Index Measure)	Suspended (see notes below)
Total Accident Rate	≤ 2.78%	2.71%
Workers' Comp: POWER Initiative Index	Meet 2 targeted POWER Initiative Goals	Met all targeted POWER initiative Goals
Telework Participation	27.5%	25.95%
Diversity and Inclusion		
Diversity in High Grades & Total Workforce	Minorities and Women at Parity	At Parity
Individuals with Targeted Disabilities	2%	1.95%
Veterans on Board	.4% increase in veterans onboard as a % of total workforce	33.08% new hired vets 38.76% disabled vets

Organizational Climate: DeCA conducted an Organizational Assessment Survey (OAS) in 2016 to assess the Agency's Organizational Climate. The OAS, which is administered by the Office of Personnel Management (OPM), is conducted biennially. Organizational Climate is used to look at the improvement of the OPM's identified "High Impact Dimensions" utilizing an Index Performance Measure approach. Based on a correlation analysis of the actual survey results, these dimensions are identified as the top predictors of turnover intentions, job satisfaction, satisfaction with the organization, and perceived customer satisfaction. DeCA has had a Memorandum of Understanding (MOU) with the Office of Personnel Management (OPM) since 2005 for periodic conduct of the

OAS. In FY 2017, DeCA developed working groups comprised of all employee levels and implemented corrective action initiatives for dimensions targeted for improvement by the FY 2016 survey results. The OAS was suspended in 2018 to reevaluate a new process and tools that better align to our business model.

Total Accident Rate: This metric indicates the rate at which accidents occur per 100 DeCA employees (U.S. citizens only). In compliance with Department of Labor, DoD, and other regulatory agencies, DeCA strives to provide a safe and healthful working environment by protecting personnel from accidental death, injury, and occupational illness. To better define the 2016 BSC goal, we performed a multi-year analysis on our accident data (2007-2015) to establish a true baseline and establish more realistic out-year goals. This assessment resulted in an upper control limit of 2.92, which we adopted as our updated baseline and 2016 goal. The out-year goals are established using a 2.5% annual reduction in the accident rate, starting from this new baseline. Total Accident Rate (TAR) base line for FY 2018 was 2.78% and the FY 2018 TAR was 2.71%, which is below the target.

Workers' Compensation – POWER Initiative Index. On July 19, 2010, former President Obama established a 4-year Protecting Our Workers and Ensuring Reemployment (POWER) Initiative, covering fiscal years 2011 through 2014. The POWER Initiative extends prior workplace safety and health efforts of the Federal Government by setting more aggressive performance targets. For the POWER Initiative Index, DeCA focused on areas encompassed by the Office of Workers' Compensation Programs (OWCP). DeCA measures the Agency's results against those focus area goals as set by Department of Labor. The focus areas are: 1) increasing the timely filing of workers' compensation claims and 2) increasing the timely filing of wage-loss claims. DeCA met all targeted POWER Initiative Goals for FY 2018.

Telework Participation: The Department of Defense's goal is to increase the visibility and usage of the telework program and to integrate and embed its use in our mainstream operations, where appropriate. As a result, DeCA is working towards the DoD goal of 30% participation by FY 2025, at least one time per pay period. Telework eligible workforce includes above-store employees, not store level commissary employees. DeCA had a 27.5% target for FY 2018 and results were 25.95%, which is slightly below target.

Diversity and Inclusion: In keeping with Executive Order 13583, establishing a Coordinated Government-wide Initiative to Promote Diversity and Inclusion in the Federal Workforce, DeCA is continuing to monitor its workforce demographic data to ensure that no barriers to employment and advancement of under-represented groups develop. DeCA has incorporated the measures below in this category to help us evaluate our progress in this area.

- **Diversity in High Grades and Total Workforce:** This measure compares DeCA's percentage of minorities and women in the overall workforce and high grades to the corresponding totals in the overall Federal workforce. DeCA's performance goal is to achieve parity (within 5% of the corresponding measure in the overall Federal workforce). DeCA continues to focus on diversity of feeder grades, GS-9 – GS-13, to ensure a quality pipeline of candidates prepared to lead DeCA in the future. FY 2018 results met the goal of at parity.

- **Individuals with Targeted Disabilities:** DeCA seeks to achieve and sustain the Federal Government’s 2 percent goal. FY 2018 results are 1.95%, which is slightly below the goal.
- **Veterans Employment Performance:** Former President Barack Obama made it a priority for the Government to employ more veterans in the Civil Service via Executive Order (13518) in 2009. As a result, the Federal Government and Department of Defense are committed to the Veterans Hiring Initiative which aims to increase the hiring of veterans into the workforce. The Veterans Employment Performance measure is an internal DeCA goal and not required by DoD or OPM. DeCA will transition to align this measure with the new DoD benchmark once assigned. DeCA’s internal goal is to increase hiring .4% each year, for a total increase of 2% by 2022. DeCA has met the goal for FY2018.

GOVERNANCE AND ACCOUNTABILITY:

DeCA continues to refine our governance and decision-making processes by improving methods that determine resource allocation and ensuring Agency investments remain strategically aligned. The Agency governance process employs a prioritization model with scoring criteria to guide the evaluation of potential investments. Enterprise-level collaboration and direct involvement of executive and senior leadership is crucial in maintaining an efficient process. Collaborative discussions minimize the layers of review and streamline the decision-making process. Good stewardship requires an agile and fiscally responsible governance process if we are to remain a model government organization.

A Continuous Process Improvement project conducted this year improved the Governance process Business Needs Statement by adding manpower requirements and clarity of information required for each submission, and increased the visibility and transparency of budget information and requirements throughout the Agency.

The Agency also continues its role as a leader in the DoD’s compliance with OMB Circular No. A-123, “*Management’s Responsibility for Enterprise Risk Management and Internal Control*” and Appendix A: “*Internal Control over Financial Reporting*.” The Appendix A methodology continues to be the basis for conducting and documenting management’s assessment of internal controls for all aspects of the Agency’s operation. DeCA has strengthened its foundation of budget and performance integration by reviewing and rebuilding processes for validation and testing of internal controls related to financial management by involving all areas and activities of the commissary system, to include trading partners.

In FY 2018, DeCA conducted an internal control assessment of the effectiveness of our ICOFR for the following implementation areas: Budgetary Resources (Appropriations Received, Accounts Payable, Accounts Receivable and Civilian Pay); Critical Assets (Inventory, Personal Property, Real Property and Cash and other Monetary Assets); and Other Long-Term Liabilities (Environmental Liability, Federal Employee Compensation Act Liability, Foreign National Separation Pay Liability). The assessment of the implementation areas was conducted in strict compliance with the OMB

Circular A-123, Appendix A, as directed by DoD guidance under the oversight of the DeCA SAT.

DeCA's Statement of Assurance for FY 2018 reported on financial and nonfinancial operations, and financial system compliance. As of July 19, 2018, DeCA's Director was able to provide an unqualified statement of reasonable assurance that DeCA's internal controls met the objectives of the FMFIA and a qualified statement of reasonable assurance for FFMIA. Ten years into the Agency's Financial Improvement Plan the methodology continues to aid in effective financial and operational processes. The Agency's embrace of this program, has resulted in cost avoidance, improved business processes, and involved functional leaders from all aspects of the organization.

CONTINUOUS PROCESS IMPROVEMENT:

DeCA continued building the foundation of its Continuous Process Improvement (CPI) program in FY18. CPI practitioners trained belt candidates, facilitated CPI events such as process mapping, and prepared the Agency for enterprise-wide CPI success in FY19 and beyond.

INNOVATION:

DeCA's Innovation Program provides employees with multiple opportunities to share ideas, present solutions, and collaborate on ways to improve commissary operations. The Improve Defense Commissary Agency's Efficiency and Service (IDEAS) program is a structured method to submit ideas for improvement, innovations, or Agency savings to a cross-functional review panel for evaluation. In FY 2018, 54 suggestions were received and considered.

SUMMARY

DeCA values its role in providing a benefit that enhances the quality of life and readiness of our military community. Embedded in our goals is the focus on building sales and offering savings while collaborating with the entire military resale community. We continue to step-up our technology capabilities to ensure we have the right products at the right price at the right time on well-stocked shelves. As a good steward of this core readiness support element, and valued part of the military benefit, it is essential to strengthen a performance-driven, results-focused, agile and accountable Agency. Efforts to continually refine our processes and culture will translate to improved results and continued relevance for our stakeholders. We are "laser-focused" on offering the best savings possible and maintaining the relevance of the commissary benefit for years to come.

This page intentionally left blank

PART III

FINANCIAL SECTION



Message from the CHIEF FINANCIAL OFFICER (CFO)

I am pleased to present the Fiscal Year (FY) 2018 Annual Financial Report (AFR). This report is a clear reflection of the unwavering commitment that the Agency and its employees endeavor to provide rigorous financial management practices and processes over commissary operations. As we continue to face uncertainty in our funding, DeCA remains focused on accountability of taxpayers' dollars while providing significant savings to our patrons and other authorized shoppers. We continue to face challenges with funding (proposed \$1B reduction by 2021), legacy system environments and ever-changing policies that govern the benefit. This includes reform initiatives that involve DeCA and the Exchanges, all of which have become increasingly complex as we move into FY 2019 and beyond.

DeCA operated under an extended Continuing Resolution (CR) during FY 18. DeCA did not receive full year appropriation until April, resulting in seven months of incremental funding to continue operations. Managing in this manner increased the workload significantly and required additional oversight to ensure our expenditures did not exceed funding allocated for each of the CR periods. With the challenges of a CR, we were able to execute over 94% of our funding, aligning with our strategy for execution. These efforts were likely transparent to our customers as every effort was made to minimize interruptions in their funding stream.

DeCA continues to push forward to meet the needs of the Agency in support of our shoppers in the most efficient manner possible. For FY 2018, a few notable accomplishments and initiatives that contributed to our successful year include:

- DeCA underwent an extensive budget data call effort to reduce and align requirements to achieve efficiencies and savings. The process was extensive, tedious and engaged every level within the Agency. This arduous effort resulted in a ~ \$65M reduction in requirements for FY 2019 that will continue through the out-years. DeCA will have a need to request additional funding in FY 2021 and beyond to support the current footprint of the Agency.
- DeCA deployed an Inventory Management Module and new Ordering System with the deployment of DAX/IM within the Enterprise Business Solution (EBS) to Ft. Eustis. This process has provided more transparency in our stockage rates and the number of mis-picks received at the store. The most important piece is the continual analytics that update the product orders based on current stockage levels and projected sales based on recent historical sales trends. The Ft. Eustis store has a real time capability for knowing what product is in stock, what is ordered and when it will be delivered. This has resulted in a smaller inventory carrying cost and less shrinkage due to expired product. We will continue our deployment through 2020.
- Vendor payments (Overseas Pacific) transitioned from GPC card payments to DFAS-SAVES payments. This transition has strengthened our internal controls within the stores and Central Distribution Center (CDC) inventory for the Pacific stores and provided additional visibility within our supply chain systems.

- Natural disasters, both CONUS and OCONUS have required DeCA to establish continuity processes and procedures to ensure continued operations and support. An “all hands on deck” posture has resulted in exceptional support to our stores and our employees affected.

This is DeCA’s 18th year being audited by an independent public accounting (IPA) firm and our first modified opinion regarding its financial statements in 17 years. Fiscal year (FY) 2018 was a year of continued transformation as we begin to operate more like commercial grocers – variably pricing items and expanding our private label brand. These transformation initiatives involved re-defining accounting and business processes to fully support DeCA’s new business model. With each new FY, DeCA continues to improve and enhance our financial management processes to ensure sustainment of our business being audited. It is a true testament to the enduring team of professionals that work many hours to safeguard and accurately report the Agency’s financial position through strict reviews, firm internal controls and explicit compliance with Federal and DoD guidance during the financial statement reporting process. As DeCA’s Chief Financial Officer, I am extremely proud of the Resource Management team and all the efforts to uphold a standard of excellence within our financial management community. I believe that together with our partners and stakeholders we can face the challenges and changes ahead because of our belief in those who wear the uniform and our desire to serve them.

MORGAN.CYNTHIA
IA.L.1229474231
Cynthia L. Morgan
Chief Financial Officer

Digitally signed by
MORGAN.CYNTHIA
Date: 2018.12.16 12:01:49 -05'00'

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
BALANCE SHEETS
As of September 30, 2018 and 2017
(amounts in thousands)**

	<u>2018</u>	<u>2017</u>
Assets		
Intragovernmental:		
Fund balance with Treasury (Note 2)	\$ 1,035,595	\$ 837,072
Accounts receivable and other	117	610
Total intragovernmental assets	<u>1,035,712</u>	<u>837,682</u>
Cash	95,375	169,732
Accounts receivable and other assets, net	31,454	38,540
Inventory, net (Note 3)	384,190	368,128
General property, plant, and equipment, net (Note 4)	781,967	804,671
Total assets	<u>\$ 2,328,698</u>	<u>\$ 2,218,753</u>
Liabilities (Note 5)		
Intragovernmental:		
Accounts payable	\$ 41,146	\$ 42,834
Accrued payroll and related liabilities	32,046	33,955
Total intragovernmental liabilities	<u>73,192</u>	<u>76,789</u>
Accounts payable	352,141	401,071
Federal Employees Compensation Act actuarial liability	131,602	135,746
Environmental liabilities	30,023	30,663
Accrued payroll and related liabilities	77,825	81,787
Total liabilities	<u>\$ 664,783</u>	<u>\$ 726,056</u>
Commitments and Contingencies (Note 9)		
Net position (Note 6)		
Unexpended appropriations	\$ 387,509	\$ 278,929
Cumulative results of operations - dedicated collections (Note 10)	1,098,945	1,093,585
Cumulative results of operations - all other funds (combined totals)	177,461	120,183
Total cumulative results of operations	<u>1,276,406</u>	<u>1,213,768</u>
Total net position	<u>\$ 1,663,915</u>	<u>\$ 1,492,697</u>
Total liabilities and net position	<u>\$ 2,328,698</u>	<u>\$ 2,218,753</u>

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
STATEMENTS OF NET COST
For the Years Ended September 30, 2018 and 2017
(amounts in thousands)**

	<u>2018</u>	<u>2017</u>
Program costs:		
Gross costs	\$ 6,247,015	\$ 6,636,008
Less: Earned revenue	<u>(4,960,211)</u>	<u>(5,193,790)</u>
Net cost of operations (Notes 7 and 11)	<u>\$ 1,286,804</u>	<u>\$ 1,442,218</u>

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

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
STATEMENTS OF CHANGES IN NET POSITION
For the Years Ended September 30, 2018 and 2017
(amounts in thousands)**

	2018			2017		
	Dedicated Collections	All Other Funds	Consolidated Total	Dedicated Collections	All Other Funds	Consolidated Total
Unexpended Appropriations:						
Beginning Balance	\$ -	\$ 278,929	\$ 278,929	\$ -	\$ 487,715	\$ 487,715
Budgetary Financing Sources						
Appropriation transfer in/out	-	1,389,340	1,389,340	-	1,214,045	1,214,045
Other adjustments (recissions)	-	(47)	(47)	-	(22)	(22)
Appropriations transfers used	-	(1,280,713)	(1,280,713)	-	(1,422,809)	(1,422,809)
Total Budgetary Financing Sources	-	108,580	108,580	-	(208,786)	(208,786)
Total Unexpended Appropriations (Note 6)	\$ -	\$ 387,509	\$ 387,509	-	278,929	278,929
Total Net Position (Note 6)	<u>\$ 1,098,945</u>	<u>\$ 564,970</u>	<u>\$ 1,663,915</u>	<u>\$ 1,093,585</u>	<u>\$ 399,112</u>	<u>\$ 1,492,697</u>
Cumulative Results of Operations:						
Beginning balance	<u>\$ 1,093,585</u>	<u>\$120,183</u>	<u>\$ 1,213,768</u>	<u>\$ 1,165,660</u>	<u>\$15,921</u>	<u>\$ 1,181,581</u>
Budgetary Financing Sources						
Appropriations transfers used	-	1,280,713	1,280,713	-	1,422,809	1,422,809
Non-exchange revenue	-	21,222	21,222	-	20,696	20,696
Other Financing Sources (Uses)						
Imputed financing (Note 7)	-	47,505	47,505	-	30,900	30,900
Transfers in (out) without reimbursement	2,397	(2,397)	-	2,364	(2,364)	-
Other Financing Sources (Uses)	-	2	2	-	-	-
Total Financing Sources	2,397	1,347,045	1,349,442	2,364	1,472,041	1,474,405
Net Cost of Operations	(2,963)	1,289,767	1,286,804	74,439	1,367,779	1,442,218
Net Change	5,360	57,278	62,638	(72,075)	104,262	32,187
Cumulative Results of Operations (Notes 6 and 10)	<u>\$ 1,098,945</u>	<u>\$ 177,461</u>	<u>\$ 1,276,406</u>	<u>\$ 1,093,585</u>	<u>\$ 120,183</u>	<u>\$ 1,213,768</u>

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

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
COMBINED STATEMENTS OF BUDGETARY RESOURCES**

For the Years Ended September 30, 2018 and 2017

(amounts in thousands)

The

	2018	2017
Budgetary Resources:		
Unobligated balance brought forward, Oct 1	\$ 230,844	\$ 423,914
Recoveries of prior year obligations	-	527
Other changes in unobligated balance	-	(549)
	230,844	423,892
Unobligated balance from prior year budget authority, net	230,844	423,892
Appropriations (discretionary and mandatory) (Note 8)	1,389,340	1,214,045
Contract authority (discretionary and mandatory) (Note 8)	4,689,687	4,824,887
Spending authority from offsetting collections (discretionary and mandatory)	248,027	267,332
	\$ 6,557,898	\$ 6,730,156
Total budgetary resources		
Status of Budgetary Resources:		
New obligations and upward adjustments (total) (Note 11)	\$ 6,246,638	\$ 6,499,265
Unobligated balances, end of year:		
Apportioned, unexpired accounts	310,332	229,917
Expired unobligated balance, end of year	928	974
	311,260	230,891
Unobligated balance, end of year (total)	\$ 6,557,898	\$ 6,730,156
Total budgetary resources		
Outlays, net		
Outlays, gross (discretionary and mandatory)	\$ 6,243,019	\$ 6,506,824
Actual offsetting collections (discretionary and mandatory)	(5,052,248)	(5,127,407)
	\$ 1,190,771	\$ 1,379,417
Agency outlays, net (discretionary and mandatory)		

accompanying notes are an integral part of the financial statements.

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS
(Except as noted, all dollar amounts are in thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Description of Reporting Entity

The Defense Commissary Agency (DeCA) provides grocery, meat, and produce items to members of the U. S. Armed Forces, their dependents, retirees, reservists, Guard members, 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. The Statements of Net Cost presents the cost of DeCA's mission to 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 war fighters' peace of mind, knowing their families have secure and affordable access to American products.

DeCA, with its headquarters located at Fort Lee (near Petersburg), Virginia, has five area offices in the East, Central, West, Europe, and Pacific. DeCA operations are financed primarily by a Working Capital Fund (WCF) and Surcharge Collections Trust Fund.

DeCA's WCF is considered part of the DoD's Defense-wide WCF, which includes the financial activities 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 funds 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 finances the operating cost of retail stores, agency and region headquarters, field operating activities, and support services. The primary revenue source for this activity group is a direct appropriation from Congress 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.

The Surcharge Collections Trust Fund is part of DeCA's general funds (GF).

DeCA's Surcharge Collections Trust Fund is funded primarily by a five percent surcharge applied to each sale. This fund, established by law as the repository for the surcharge collected on the cost of commissary goods paid for by authorized patrons, primarily finances DeCA's store-level information management equipment and support, and construction programs. As the use of resources associated with the Surcharge Collections Trust Fund is limited by public law, this fund has been identified as a fund from dedicated collections.

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS
(Except as noted, all dollar amounts are in thousands)

B. Basis of Presentation and Accounting

These financial statements have been prepared to report the financial position, net cost of operations, changes in net position, and sources and availability of budgetary resources. The financial statements have been prepared from the books and records of DeCA in accordance with accounting principles generally accepted in the United States (U.S.) and DoD accounting policies, which are summarized in this note.

Transactions are recorded on both an accrual accounting basis and budgetary accounting 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. Liabilities not covered by budgetary resources represent amounts owed in excess of available appropriated funds. The liquidation of liabilities not covered by budgetary resources is dependent on future congressional appropriations.

The presentation of the Status of Budgetary Resources was streamlined pursuant to revisions in Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*.

C. Fund Balance with Treasury (FBWT)

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

D. Cash

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

E. Accounts Receivable

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 deemed necessary for Federal accounts receivable.

Receivables from the public generally arise from manufacturer-related transactions, which are associated with 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 the age of outstanding balances. The allowance is adjusted accordingly at the time of collection or write-off during the fiscal year.

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS
(Except as noted, all dollar amounts are in thousands)

F. Inventory, Net

Inventory consists primarily of grocery, meat and produce items and is held for sale to authorized commissary patrons. DeCA purchases inventory at the lowest possible cost, and such inventory is recorded in its accounting records at latest acquisition cost (LAC) plus a 1% mark-up.

Inventory balances for each store are adjusted based on aggregate purchases and sales (adjusted to account for the 1% mark-up), transfers and other adjustments. Store managers are expected to maintain and update operating system data of product level inventories but this information is not used to support reported balances. Prior to FY2018, DeCA performed dollar value inventories reflective of shelf price (cost plus 1%) annually at each commissary and Central Distribution Center (CDC). Store inventories values were adjusted based on the results of these inventories. Monthly adjustments are posted to an allowance account to inventory values to reflect estimates of normal inventory loss or “shrinkage” based on 1% of the receipts paid for the month.

In order to maintain a cost plus 1% inventory valuation under new variable pricing strategies, a monthly adjustment is made to the book value by store for the net aggregate change of shelf prices from the calculated shelf price of cost plus 1% methodology to eliminate changes in book value due to changes in pricing at the product level.

In FY2018, DeCA initiated the migration of its legacy inventory business system to a fully integrated grocery ordering and inventory management system, called Enterprise Business Solution, or EBS. This new system also moves DeCA in the direction of utilizing a true perpetual inventory methodology. In order to facilitate changes in inventory requirements, DeCA suspended its shelf price inventory valuation formal inventories in order to develop the proper perpetual requirements via inventory testing models at specified stores, as well as overcome technical constraints from bridging legacy and new systems in the inventory valuation process. All stores have maintained their monthly cyclical counts and recording of adjustments for estimated shrinkage.

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

General Property, Plant and Equipment (PP&E) consists of buildings, structures and facilities (BSF), software, equipment and construction-in-progress. PP&E is stated at acquisition cost, less accumulated depreciation/amortization. DoD establishes capitalization and depreciation policies for PP&E.

DoD Financial Management Regulation accounting policy requires assets to be reported on the financial statement of the entity which controls access to the economic benefit of the asset. Since DeCA controls access to the economic benefit of the commissaries in which it operates, such buildings and equipment financed or otherwise obtained by other DoD agencies, are transferred to DeCA upon construction completion. Such transfer shall be recorded as a Transfer In in the Statement of Net Position.

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS
(Except as noted, all dollar amounts are in thousands)

PP&E acquisitions are capitalized if they have an estimated useful life of two or more years, are not intended for sale in the ordinary course of operations, are acquired or constructed with the intention of being used or being available for use by the entity, and meet the capitalization threshold of \$250. This capitalization threshold applies to asset acquisitions and modifications/improvements placed into service after September 30, 2013. PP&E acquired prior to October 1, 2013 were capitalized at prior threshold levels (\$100 for equipment and \$20 for real property).

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 currently forty-five years for BSF and five to ten years for software and equipment. The actual commencement of depreciation is based on the midyear convention method for buildings. Under the midyear convention method, six months of depreciation is computed and expensed in the first and last year of an asset's useful life regardless of the actual month an asset was placed in or removed from service. The month available for service method is used for all other capital assets.

When DeCA funds the acquisition of real property in a host nation or in the United States, and meets the DoD Financial Management Regulation accounting policy outlined above, it reports the asset in its financial statements. If DeCA buildings, structures or facilities are eventually closed, losses are recorded for the net book value of the assets at the time of closure.

H. Accrued Payroll and Related Liabilities

Accrued payroll and related liabilities consist of payments DeCA owes to the Department of Labor (DOL) for workers' compensation paid under 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 the respective Federal agencies for those paid claims. The actuarially determined liability related to workers' compensation is described in Note 1.I.

Accrued Payroll and Benefits. Accrued payroll and benefits includes the portion of employee compensation earned, but not paid, at the end of the reporting period 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.

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS
(Except as noted, all dollar amounts are in thousands)

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 accrued leave earned, but not taken, funding will be obtained from future financing sources.

I. Actuarial Liability

In addition to the liabilities discussed above, DeCA records an actuarial liability for its 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. 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 related to Federal retirement plans, health benefits, and life insurance.

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.

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 OPM. DeCA recognizes an imputed financing source 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.

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS
(Except as noted, all dollar amounts are in thousands)

K. Environmental Liabilities

DeCA's environmental liabilities reflect the potential liability associated with the clean-up and removal of environmentally hazardous materials, primarily asbestos and lead based paints in DeCA's facilities. DeCA estimates its environmental liability based on the number of facilities constructed before 1988 that have not been remediated. 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.

The environmental liabilities for the DeCA are based on accounting estimates which require certain judgments and assumptions that are reasonably based upon information available at the time the estimates are calculated.

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 difference between revenues over expenses and transfers to Treasury in the WCF and GF since inception.

M. Nonexchange Revenue

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

N. Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amount of assets and liabilities at the date of the financial statements, and the amount of revenues and costs reported during the period. Actual results could differ from those estimates, and the difference will be adjusted for and included in the financial statements in the year such differences are determined.

O. Commitments and Contingencies

DeCA is a party in various administrative proceedings, legal actions, and potential claims. In the opinion of DeCA management and legal counsel, the ultimate resolution of these proceedings, actions, and claims will not materially affect the financial position or results of

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**
(Except as noted, all dollar amounts are in thousands)

operations of DeCA. Contingent liabilities are recognized when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

NOTE 2 - FUND BALANCE WITH TREASURY

FBWT consists of three types of funds – appropriated funds, revolving funds, and trust funds. The appropriated funds include commissary operations and military construction; the revolving fund relates to DeCA’s commissary resale stocks fund, and the trust fund relates to the Surcharge Collections Trust Fund.

The following table shows the balance for each type of fund as of September 30, 2018 and 2017:

Fund balances:	2018	2017
Appropriated funds		
General Fund	\$ 928	\$ 974
Working Capital Fund	571,134	488,590
Total	<u>572,062</u>	<u>489,564</u>
Revolving funds		
General Fund	-	-
Working Capital Fund	33,828	(55,420)
Total	<u>33,828</u>	<u>(55,420)</u>
Trust funds	429,705	402,928
Total	<u>\$ 1,035,595</u>	<u>\$ 837,072</u>

The following table shows the status of the fund balances as of September 30, 2018 and 2017.

	2018			
Status of fund balances:	Appropriated	Revolving	Trust	Total
Unobligated balance available	\$ 282,093	\$ -	\$ 28,239	\$ 310,332
Unobligated balance unavailable	928	-	-	928
Obligated balance not yet disbursed, net of contract authority	289,041	33,828	401,466	724,335
Totals	<u>\$ 572,062</u>	<u>\$ 33,828</u>	<u>\$ 429,705</u>	<u>\$ 1,035,595</u>

	2017			
Status of fund balances:	Appropriated	Revolving	Trust	Total
Unobligated balance available	\$ 176,480	\$ -	\$ 53,437	\$ 229,917
Unobligated balance unavailable	974	-	-	974
Obligated balance not yet disbursed, net of contract authority	312,110	(55,420)	349,491	606,181
Totals	<u>\$ 489,564</u>	<u>\$ (55,420)</u>	<u>\$ 402,928</u>	<u>\$ 837,072</u>

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**
(Except as noted, all dollar amounts are in thousands)

Unobligated balance is classified as available or unavailable and represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. The unavailable balance consists primarily of funds invested in Treasury securities that are temporarily precluded from obligation by law. Unavailable appropriated balances represent amounts that have not been apportioned by OMB for use. Unobligated balances for trust fund accounts are restricted for use by public law that established the funds.

Obligated balance not yet disbursed generally represents funds that have been obligated for goods and services not received, and those received but not paid.

DeCA is a revolving fund activity and because the total activity group remains positive, the negative balance remains within statutory compliance.

NOTE 3 - INVENTORY, NET

The following table summarizes net inventory for September 30, 2018 and 2017:

	2018
Inventory LAC without estimate for losses incurred	\$ 411,520
Estimate for losses incurred	<u>(24,911)</u>
Inventory on hand at LAC	386,609
Unrealized holding gain (loss)	<u>(2,419)</u>
Inventory, Net	<u><u>\$ 384,190</u></u>
	2017
Inventory LAC without estimate for losses incurred	\$ 382,236
Estimate for losses incurred	<u>(11,462)</u>
Inventory on hand at LAC	370,774
Unrealized holding gain (loss)	<u>(2,646)</u>
Inventory, Net	<u><u>\$ 368,128</u></u>

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**
(Except as noted, all dollar amounts are in thousands)

NOTE 4 – GENERAL PROPERTY, PLANT AND EQUIPMENT, NET

General property, plant and equipment (PP&E) at September 30, 2018 and 2017 is summarized as follows:

	2018		
PP&E category	Acquisition Value	Accumulated Depreciation	Net
Buildings, structures, and facilities	\$ 2,268,846	\$ (1,590,787)	\$ 678,059
Software	42,181	(30,982)	11,199
Equipment and other assets	214,546	(168,926)	45,620
Construction-in-progress	47,089	-	47,089
Totals	\$ 2,572,662	\$ (1,790,695)	\$ 781,967
	2017		
PP&E category	Acquisition Value	Accumulated Depreciation	Net
Buildings, structures, and facilities	\$ 2,258,835	\$ (1,559,187)	\$ 699,648
Software	45,403	(30,727)	14,676
Equipment and other assets	212,988	(156,453)	56,535
Construction-in-progress	33,812	-	33,812
Totals	\$ 2,551,038	\$ (1,746,367)	\$ 804,671

In July 2016, a new Commissary was built and funded by a non-Federal entity; however ownership of such commissary is expected to be transferred to DoD's United States Marine Corps (USMC). Once the transfer from the non-Federal entity to the USMC is complete, that ownership will then be transferred to DeCA, as required by DoD policy. Until the transactions are complete, DeCA cannot record the commissary building as an asset in its financial statements.

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS
(Except as noted, all dollar amounts are in thousands)

The following table summarizes current and noncurrent other liabilities as of September 30, 2018 and 2017:

	2018		
	Current Liabilities	Non-Current Liabilities	Total
<u>Other liabilities</u>			
Intragovernmental:			
Workers compensation	\$ 12,249	\$ 15,737	\$ 27,986
Employer contributions and payroll taxes payable	4,060	-	4,060
Subtotal	16,309	15,737	32,046
With the public:			
Accrued funded payroll and benefits	24,210	-	24,210
Foreign national separation pay	10,106	-	10,106
Accrued leave	43,509	-	43,509
Subtotal	77,825	-	77,825
Totals	\$ 94,134	\$ 15,737	\$ 109,871
2017			
	Current Liabilities	Non-Current Liabilities	Total
<u>Other liabilities</u>			
Intragovernmental:			
Workers compensation	\$ 14,196	\$ 15,570	\$ 29,766
Employer contributions and payroll taxes payable	4,189	-	4,189
Subtotal	18,385	15,570	33,955
With the public:			
Accrued funded payroll and benefits	23,705	-	23,705
Foreign national separation pay	14,360	-	14,360
Accrued leave	43,722	-	43,722
Subtotal	81,787	-	81,787
Totals	\$ 100,172	\$ 15,570	\$ 115,742

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**
(Except as noted, all dollar amounts are in thousands)

NOTE 6 - NET POSITION

The following table summarizes the net position by fund type as of September 30, 2018 and 2017:

	2018		
	General Funds	Working Capital Funds	Total
Net position:			
Unexpended appropriations	\$ 928	\$ 386,581	\$ 387,509
Cumulative results of operations - dedicated collections	1,098,945	-	1,098,945
Cumulative results of operations - other funds	-	177,461	177,461
Total cumulative results of operations	<u>1,098,945</u>	<u>177,461</u>	<u>1,276,406</u>
Totals	<u><u>\$ 1,099,873</u></u>	<u><u>\$ 564,042</u></u>	<u><u>\$ 1,663,915</u></u>
	2017		
	General Funds	Working Capital Funds	Total
Net position:			
Unexpended appropriations	\$ 974	\$ 277,955	\$ 278,929
Cumulative results of operations - dedicated collections	1,093,585	-	1,093,585
Cumulative results of operations - other funds	-	120,183	120,183
Total cumulative results of operations	<u>1,093,585</u>	<u>120,183</u>	<u>1,213,768</u>
Totals	<u><u>\$ 1,094,559</u></u>	<u><u>\$ 398,138</u></u>	<u><u>\$ 1,492,697</u></u>

NOTE 7 - IMPUTED FINANCING

The imputed financing and cost for employee benefits as of September 30, 2018 and 2017 is summarized below:

<u>Benefit Category</u>	<u>2018</u>	<u>2017</u>
CSRS/FERS	\$ 10,779	\$ 3,369
FEHB	36,595	27,428
FEGLI	105	103
Judgement Fund	26	-
Total	<u><u>\$ 47,505</u></u>	<u><u>\$ 30,900</u></u>

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS
(Except as noted, all dollar amounts are in thousands)

NOTE 8 - COMBINED STATEMENTS OF BUDGETARY RESOURCES

The Statement of Budgetary Resources (SBR) is a combined statement and, as such, intra-entity transactions have not been eliminated. The combined SBR 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 SBR has been adjusted for actual results. As such, the FY 2018 SBR may differ from the amounts in the President's Budget by the differences between estimates used for the SF 133 and the actual results reporting in the SBR.

The FY 2018 actual amounts as shown on the FY 2020 President's Budget were not available at the time the financial statements were prepared. The FY 2020 President's Budget is expected to be available in February 2019. Both documents can be located at the OMB website (<http://www.whitehouse.gov/omb>). The actual amounts reported in the FY 2017 SBR are in agreement with the actual amounts reported for the DeCA WCF in the President's FY 2018 budget request.

Total budget authority in FY 2018 and FY 2017 included appropriation transfers in the amounts of \$1,389,340 and \$1,214,045, respectively, and contract authority in the amounts of \$4,689,687 and \$4,824,887 respectively. The appropriation transfer is offset by the contract authority liquidation and is available indefinitely. Contract authority primarily provides DeCA the ability to purchase grocery, meat, and produce items for resale to authorized commissary patrons. Spending authority from offsetting collections results primarily from the sale of grocery, meat, and produce items.

Undelivered orders as of September 30, 2018 and September 30, 2017 were \$516,633 and \$463,297, respectively. Working Capital Fund intragovernmental budgetary resources for undelivered orders at September 30, 2018 were \$37,133 while nonfederal budgetary resources for undelivered orders were \$123,722. General Fund intragovernmental budgetary resources for undelivered orders at September 30, 2018 were \$192,378 while nonfederal budgetary resources for undelivered orders were \$163,400.

DeCA has no direct obligations and no reimbursable obligations in Category A which represents amounts apportioned by time period.

DeCA has \$1,293 million direct obligations apportioned under Category B. Reimbursable obligations of \$4,955 million are apportioned under Category B, which represents amounts apportioned by activity, projects or object.

The SBR includes intra-entity transactions which are not eliminated because the statements are presented as combined. There are no legal arrangements affecting the use of unobligated balances.

NOTE 9 – COMMITMENTS AND CONTINGENCIES

DeCA has no capital leases, and future non-cancelable lease payments for operating leases are not material to DeCA's financial statements.

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS**
(Except as noted, all dollar amounts are in thousands)

DeCA is a party in various administrative proceeding and legal actions related to claims for environmental damage, equal opportunity matters and contractual bid protests. DeCA has not accrued or disclosed any amounts for contingent liabilities as potential losses have not been determined to be probable or reasonably possible.

NOTE 10 – DEDICATED COLLECTIONS

The following table presents condensed data relating to DeCA’s Dedicated Collections, the Surcharge Collections Trust Fund, as of and for the years ended September 30, 2018 and 2017:

Balance Sheet	2018	2017
Assets:		
Fund balance with Treasury (Note 2)	\$ 429,705	\$ 402,928
Cash and accounts receivable	4,568	9,642
Property, plant, and equipment	711,729	731,283
Total assets	<u>\$ 1,146,002</u>	<u>\$ 1,143,853</u>
Liabilities:		
Accounts payable	\$ 17,034	\$ 19,605
Environmental liabilities	30,023	30,663
Total liabilities	47,057	50,268
Cumulative results of operations	1,098,945	1,093,585
Total liabilities and net position	<u>\$ 1,146,002</u>	<u>\$ 1,143,853</u>
Statement of Net Cost		
Program costs	\$ 238,629	\$ 330,431
Earned revenue	(241,592)	(255,992)
Net income (loss) from operations	<u>\$ (2,963)</u>	<u>\$ 74,439</u>

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
NOTES TO THE FINANCIAL STATEMENTS
(Except as noted, all dollar amounts are in thousands)

NOTE 11 - RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

The following table presents DeCA's reconciliation of net cost of operations to budgetary resources as of and for the years ended September 30, 2018 and 2017:

Resources used to finance activities	2018	2017
Budgetary resources obligated:		
New obligations and upward adjustments	\$ 6,246,638	\$ 6,499,265
Less: Spending authority from offsetting collections and recoveries	<u>(5,052,436)</u>	<u>(5,127,562)</u>
Obligations, net of offsetting collections and recoveries	<u>1,194,202</u>	<u>1,371,703</u>
Other resources:		
Imputed financing from costs absorbed by others (Note 8)	47,505	30,900
Other - Gain (losses) in capital assets	<u>2</u>	<u>-</u>
Net other resources used to finance activities	<u>47,507</u>	<u>30,900</u>
Total resources used to finance activities	<u>1,241,709</u>	<u>1,402,603</u>
Resources used to finance items not part of net costs of operations		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:		
Undelivered orders	(53,336)	50,752
Unfilled customer orders	(25)	(649)
Resources that fund expenses recognized in prior periods	(11,030)	(11,549)
Resources that finance the acquisition of assets	(4,687,345)	(4,918,204)
Other Resources that do not affect net cost of operations	(2)	-
Total resources used to finance items not part of the net cost of operations	<u>(4,751,738)</u>	<u>(4,879,650)</u>
Total resources used to finance the net cost of operations	<u>(3,510,029)</u>	<u>(3,477,047)</u>
Components of the net cost of operations that will not require or generate resources in the current year		
Components requiring or generating resources in future periods	82,208	(92,123)
Components not requiring or generating resources in future periods:		
Cost of goods sold	4,646,210	4,918,329
Depreciation and amortization	58,018	65,290
Revaluation of assets/liabilities	(10,729)	2,901
Non-exchange revenue and other	<u>21,126</u>	<u>24,868</u>
Total components of net cost of operations that will not require or generate resources in the current period	<u>4,796,833</u>	<u>4,919,265</u>
Net cost of operations	<u>\$ 1,286,804</u>	<u>\$ 1,442,218</u>

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
REQUIRED SUPPLEMENTARY INFORMATION
COMBINING SCHEDULE OF BUDGETARY RESOURCES
For the Year Ended September 30, 2018
(amounts in thousands)**

	<u>Defense Working Capital Funds</u>		<u>General Funds</u>		
	<u>Operations</u>	<u>Resale</u>	<u>Surcharge</u>	<u>Military Construction</u>	<u>Combined</u>
Budgetary Resources:					
Unobligated balance brought forward, Oct 1	\$ 176,479	\$ -	\$ 53,437	\$ 928	\$ 230,844
Recoveries of prior year obligations	-	-	-	-	-
Other changes in unobligated balance	-	-	-	-	-
Unobligated balance from prior year budget authority, net	176,479	-	53,437	928	230,844
Appropriations (discretionary and mandatory) (Note 9)	1,389,340	-	-	-	1,389,340
Contract authority (discretionary and mandatory) (Note 9)	9,773	4,679,914	-	-	4,689,687
Spending authority from offsetting collections (discretionary and mandatory)	9,077	-	238,950	-	248,027
Total budgetary resources	\$ 1,584,669	\$ 4,679,914	\$ 292,387	\$ 928	\$ 6,557,898
Status of Budgetary Resources:					
New obligations and upward adjustments (total) (Note 12)	\$ 1,302,576	\$ 4,679,914	\$ 264,148	\$ -	\$ 6,246,638
Unobligated balances, end of year:					
Apportioned, unexpired accounts	282,093	-	28,239	-	310,332
Unexpired unobligated balance, end of year	282,093	-	28,239	-	310,332
Expired unobligated balance, end of year	-	-	-	928	928
Unobligated balance, end of year (total)	282,093	-	28,239	928	\$ 311,260
Total budgetary resources	\$ 1,584,669	\$ 4,679,914	\$ 292,387	\$ 928	\$ 6,557,898
Outlays, Net					
Outlays, gross (discretionary and mandatory)	\$ 1,326,788	\$ 4,703,273	\$ 212,958	\$ -	\$ 6,243,019
Actual offsetting collections (discretionary and mandatory)	(19,993)	(4,792,521)	(239,734)	-	(5,052,248)
Agency outlays, net (discretionary and mandatory)	\$ 1,306,795	\$ (89,248)	\$ (26,776)	\$ -	\$ 1,190,771

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
REQUIRED SUPPLEMENTARY INFORMATION
COMBINING SCHEDULE OF BUDGETARY RESOURCES
For The Year Ended September 30, 2017
(amounts in thousands)**

	<u>Defense Working Capital Funds</u>		<u>General Funds</u>		<u>Combined</u>
	<u>Operations</u>	<u>Resale</u>	<u>Surcharge</u>	<u>Military Construction</u>	
Budgetary Resources:					
Unobligated balance brought forward, Oct 1	\$ 352,932	\$ -	\$ 69,986	\$ 996	\$ 423,914
Recoveries of prior year obligations	520	7	-	-	527
Other changes in unobligated balance	(520)	(7)	-	(22)	(549)
Unobligated balance from prior year budget authority, net	<u>352,932</u>	<u>-</u>	<u>69,986</u>	<u>974</u>	<u>423,892</u>
Appropriations (discretionary and mandatory) (Note 9)	1,114,045	100,000	-	-	1,214,045
Contract authority (discretionary and mandatory) (Note 9)	10,925	4,813,962	-	-	4,824,887
Spending authority from offsetting collections (discretionary and mandatory)	10,979	-	256,353	-	267,332
Total budgetary resources	<u><u>\$ 1,488,881</u></u>	<u><u>\$ 4,913,962</u></u>	<u><u>\$ 326,339</u></u>	<u><u>\$ 974</u></u>	<u><u>\$ 6,730,156</u></u>
Status of Budgetary Resources:					
New obligations and upward adjustments (total) (Note 12)	\$ 1,312,401	\$ 4,913,962	\$ 272,902	\$ -	\$ 6,499,265
Unobligated balances, end of year:					
Apportioned, unexpired accounts	176,480	-	53,437	-	229,917
Expired unobligated balance	-	-	-	974	974
Unobligated balance, end of year (total)	<u>176,480</u>	<u>-</u>	<u>53,437</u>	<u>974</u>	<u>\$ 230,891</u>
Total budgetary resources	<u><u>\$ 1,488,881</u></u>	<u><u>\$ 4,913,962</u></u>	<u><u>\$ 326,339</u></u>	<u><u>\$ 974</u></u>	<u><u>\$ 6,730,156</u></u>
Outlays, Net					
Outlays, gross (discretionary and mandatory)	\$ 1,291,993	\$ 4,922,832	\$ 291,999	\$ -	\$ 6,506,824
Actual offsetting collections (discretionary and mandatory)	(19,704)	(4,854,412)	(253,291)	-	(5,127,407)
Agency outlays, net (discretionary and mandatory)	<u>\$ 1,272,289</u>	<u>\$ 68,420</u>	<u>\$ 38,708</u>	<u>\$ -</u>	<u>\$ 1,379,417</u>

**DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
REQUIRED SUPPLEMENTARY INFORMATION
DEFERRED MAINTENANCE AND REPAIRS
FOR THE YEAR ENDED SEPTEMBER 30, 2018**
(amounts in thousands)

DeCA's PP&E is under various forms of maintenance contracts. DeCA has an equipment replacement plan that schedules replacement of equipment based on its useful life. The flexibility in the Surcharge program allows DeCA to address any out of cycle maintenance or repair. DeCA engineers use a variety of tools to constantly assess facility conditions and plan for replacement or repair of any component in a facility that may be approaching the end of its useful life. Due to the nature of DeCA's maintenance cycles and funding, DeCA does not have deferred maintenance.

This page intentionally left blank



CliftonLarsonAllen LLP
CLAconnect.com

INDEPENDENT AUDITORS' REPORT

Defense Commissary Agency
Special Assistant for Commissary Operations
Chair, Financial Audit Advisory Committee

Report on the Financial Statements

We have audited the accompanying financial statements of the Defense Commissary Agency (DeCA), a component of the United States Department of Defense (DoD), which comprise the balance sheets as of September 30, 2018 and 2017, and the related statements of net cost and changes in net position, and the combined statements of budgetary resources for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

DeCA management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America (U.S.); this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the U.S.; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 19-01, *Audit Requirements for Federal Financial Statements* (OMB Bulletin 19-01). Those standards and OMB Bulletin 19-01 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.



INDEPENDENT AUDITORS' REPORT (Continued)

Basis for Qualified Opinion

As more fully described in Note 1 to the financial statements, DeCA initiated the migration of its legacy inventory business system to a commercial product for grocery ordering and inventory management and in connection with this migration ceased performing annual physical inventories at its commissaries for FY2018, which were used to support, and the basis for adjustments to, recorded inventory values for each commissary. In lieu of this key control, DeCA is developing store level perpetual inventory requirements in conjunction with this implementation.

As a result, during FY2018, DeCA did not have an established process to validate and reconcile a comprehensive set of product level inventory data maintained at each commissary with the recorded inventory balances. Quantification of the effect of this matter is not practical.

Qualified Opinion on the Financial Statements

In our opinion, except for the possible effects of the matter described in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Defense Commissary Agency as of September 30, 2018 and 2017, and its net costs, changes in net position, and budgetary resources for the years then ended, in accordance with accounting principles generally accepted in the U.S.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the U.S. require that the information in DeCA's Management Discussion and Analysis (MD&A) and other Required Supplementary Information (RSI) (Combining Schedule of Budgetary Resources and Deferred Maintenance and Repairs) in DeCA's Annual Financial Report, be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Federal Accounting Standards Advisory Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the MD&A and other RSI in accordance with auditing standards generally accepted in the U.S., which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audits of the financial statements. We do not express an opinion or provide any assurance on this supplementary information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The other information, as noted in the table of contents of DeCA's Fiscal Year 2018 Financial Report (pages 2 through 10, 28 through 36, and the Message from the Chief Financial Officer on page 39), is presented for purposes of additional analysis and is not a required part of the financial statements. In addition, management has included references to information on websites or other data outside of the Agency Financial Report. This information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

INDEPENDENT AUDITORS' REPORT (Continued)

Report on Internal Control over Financial Reporting and on Compliance Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered DeCA's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of DeCA's internal control or on management's statement of assurance on internal control included in the MD&A. Accordingly, we do not express an opinion on the effectiveness of DeCA's internal control or on management's statement of assurance on internal control included in the MD&A.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of DeCA's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did identify a deficiency in internal control, described below and in Appendix A that we consider to be a material weakness.

Controls over Inventory Need Improvement

As described in Note 1, DeCA initiated the migration of its legacy inventory business system to a new ordering and inventory management system and, in connection with this migration, ceased performing annual physical inventories at its commissaries for FY2018, which were used to support, and the basis for adjustments to the recorded inventory balances. In lieu of this key control, DeCA does not have an established process to reconcile a comprehensive set of product level inventory data maintained at each commissary with the recorded inventory balances.

In addition, our testing of inventory quantities identified erroneous data and significant variances between actual product quantities and the quantities recorded in the legacy inventory business system. Although stores do perform monthly cycle counts, DeCA does not have a structured process for stores to track and monitor all product level quantities maintained within the legacy inventory business system to ensure the accuracy of all inventory data for each store.

We made recommendations to DeCA management to ensure these controls are properly designed in connection with its inventory system migration efforts.

Compliance

As part of obtaining reasonable assurance about whether the DeCA's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct effect on the determination of material

INDEPENDENT AUDITORS' REPORT (Continued)

financial statement amounts and disclosures. The results of our tests disclosed one instance of noncompliance, described below and in Appendix B, which is required to be reported under *Government Auditing Standards*.

DeCA's Financial Management Systems Do Not Comply with Federal Requirements

DeCA relies on a large portfolio of DeCA-owned and Department of Defense (DoD)-owned and operated systems. Most of DeCA's proprietary mission critical business and financial systems are supported by aging and outdated technology, and are in need of replacement to address performance, flexibility, and system interface issues.

DeCA also uses two separate DoD-owned accounting systems to process financial transactions. Neither system is able to process transactions in accordance with the United States Standard General Ledger (USSGL) at the transaction level, resulting in the need to apply extensive manual processes (journal entries outside feeder systems) to adjust balances in those systems prior to DeCA preparing its consolidated financial statements.

While transformation efforts are now underway, this process is expected to take several years to complete. DeCA's complete migration to a new compliant DoD-owned accounting system is currently scheduled for 2021.

Management's Responsibility for Internal Control and Compliance

Management is responsible for (1) evaluating the effectiveness of internal control over financial reporting based on criteria established under the Federal Managers' Financial Integrity Act of 1982 (FMFIA), (2) providing a statement of assurance on the overall effectiveness on internal control over financial reporting, and (3) complying with laws, regulations, contracts and grant agreements.

Auditors' Responsibility

We are responsible for obtaining a sufficient understanding of internal controls over financial reporting to plan the audit and testing compliance with certain provisions of laws, regulations, contracts, and grant agreements.

We did not evaluate all internal controls relevant to operating objectives as broadly established by FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to controls over financial reporting. Because of inherent limitations in internal control, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected. We also caution that projecting our audit results to future periods is subject to risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate. In addition, we caution that our internal control testing may not be sufficient for other purposes.

We did not test compliance with all laws, regulations, and contracts applicable to DeCA. We limited our tests to certain provisions of laws, regulations, contracts and grants noncompliance with which could have a direct effect on the determination of material financial statement amounts and disclosures. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

INDEPENDENT AUDITORS' REPORT (Continued)

Status of Prior Year Control Deficiencies and Noncompliance Issues

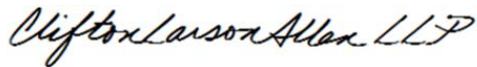
We have reviewed the status of DeCA's corrective actions with respect to the findings included in the prior year's Independent Auditors' Report, dated December 27, 2017. The status of prior year findings is presented in Exhibit C.

Management's Response to Findings

Management's response to the findings identified in our report is presented in Exhibit D. We did not audit DeCA's response and, accordingly, we express no opinion on it.

Purpose of the Report on Internal Control over Financial Reporting and on Compliance

The purpose of the Report on Internal Control over Financial Reporting and on Compliance is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of DeCA's internal control or on compliance. These reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering DeCA's internal control and compliance. Accordingly, these reports are not suitable for any other purpose.



CliftonLarsonAllen LLP
Arlington, Virginia
November 8, 2018

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT A
Material Weakness

Controls over Inventory Need Improvement

The Defense Commissary Agency (DeCA) needs to improve its internal controls over the validation and reconciliation of commissary inventory data. During fiscal year 2018, DeCA initiated the migration of its inventory business system to a commercial product for grocery ordering and inventory management and in connection with this migration, ceased performing annual physical inventories at its commissaries. These annual physical inventories served as a key control to ensuring the balances of their recorded inventories were complete and accurate. While individual commissary staff do monitor and update inventory quantities reported in the legacy inventory business system, DeCA does not have an established process to validate and reconcile the complete product level inventory data population maintained at each commissary with the recorded inventory balances reported in the general ledger.

In connection with our testing of the product level inventory data at a sample of commissaries, DeCA generated custom reports from their inventory management system that integrated current inventory quantities with product level unit cost data for each selected commissary.

In our review of these reports, we noted various products with unusually high quantities. In discussions with the store managers, we confirmed that many of these products were no longer in stock and the recorded quantities were in error. In researching this, we determined that most of the erroneous data related to pallets of grocery items, and shippers, which are self contained store displays containing multiple grocery items. These bulk items have their own unique product code. We determined that these pallets and shippers were added to the store's inventory when received, but when the stock is broken down and moved to the store floor, the individual grocery items were added to the store's inventory; however, the quantity of the pallet or shipper in the store's inventory was not correspondingly reduced.

We also found other anomalous data with seasonal and bulk items, such as loose candy. DeCA has agreements with vendors for the return and refund of certain unsold stock items. The quantities in the inventory system are not always reduced when these items are returned. Other high turnover items where vendor staff deliver and stock the quantities required (direct store delivery) were not tracked in the legacy system at all.

In order to evaluate the reliability of the remaining data, we excluded these anomalous data and selected other grocery items for testing. In our testing of non-anomalous data across 10 commissaries of varying size, we found 67% of the items selected for testing had actual quantities that differed from the recorded quantities in the inventory management system and 72% of the items with variances had variances in excess of 10% from the recorded quantities.

Without accurate data on inventory quantities, DeCA is not able to adequately support the balance of its inventory reported in its accounting records. Accurate inventory data is also critical for effective stock management as inventory on hand is a key determinant in initiating vendor orders.

Management did not report this weakness in their management assurance statement prepared in connection with their evaluation of internal controls performed in accordance with OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*.

In connection with its migration to its new ordering and inventory management system, we recommend DeCA:

1. Develop standard comprehensive inventory reports that are generated for the review and analysis by store managers.
2. Ensure pallets and shippers are removed from the inventory system when broken down.
3. Ensure inventory quantities are properly adjusted for vendor returns.

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT A
Material Weakness

4. Review the policies and procedures for performing and reporting on regular random inventory counts at the product level.
5. Review the process for accounting for direct ship and delivery (DSD) items
6. Review allowable tolerance levels based on store size, and DeCA's guidance for addressing out of tolerance situations based on results of periodic cycle counts.
7. Establish procedures for the comparison of product level inventory reports to the general ledger balances, taking into account normal timing differences and shrinkage adjustments.

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT B
Noncompliance

Noncompliance with the Federal Financial Management System Requirements

The Defense Commissary Agency (DeCA) relies on a large portfolio of DeCA-owned and Department of Defense (DoD)-owned and operated systems. Most of DeCA's proprietary mission critical business and financial systems are supported by aging and outdated technology, and are in need of replacement to address performance, flexibility, and system interface issues. While transformation efforts are now underway, this process is expected to take several years to complete. The Enterprise Business System (EBS) is DeCA's replacement system for inventory purchasing and management, which will contain various integrated modules for various resale business activities of DeCA.

A summary of the various business processes, current and planned supporting systems, and status of their implementation is presented below.

Business Process	Current System	Future System	Status	Comment
Resale supply ordering/cost management	DIBS	DAX (EBS)	Migration in Process	Expect to be completed in 2020
Inventory management	DIBS	IM (EBS)	Migration in process	Expect to be completed in 2020
Distribution Center Inventory Management	WMS	-	Migration in process	Expect to be completed in 2019
Voucher/coupon management	SAVES	EBS	-	-
Vendor credit/return management	AVCM	EBS	Migration in process	Automated credits migrated
Revenue/sales management	CARTS	-	-	-
Personnel management	DCPDS	-	-	SOC effective
Timekeeping	TAS	-	-	Testing at stores
Payroll management	DCPS	-	-	SOC effective
Property Management	DPAS	-	-	SOC effective
Travel Management	DTS	-	-	SOC effective
Procurement/contract management	DBMS	DAI	-	SOC effective
Voucher management	iRAPT	-	-	SOC effective
Disbursements	ADS	-	-	SOC effective
Financial accounting	DBMS/ STANFINS	DAI	In planning	Planned for 2021
Financial reporting	DDRS	-	-	SOC effective with findings

DeCA uses two separate DoD-owned accounting systems (DBMS and STANFINS) to process financial transactions that were developed and implemented prior to the establishment of current federal financial management system requirements. DBMS accounts for transactions associated with the appropriated funds and surcharge collections and STANFINS accounts for all resale inventory transactions. These systems are not interfaced, and do not comply with Federal financial

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT B (Continued)

management systems requirements or the application of the United States Standard General Ledger (USSGL) at the transaction level. These limitations affect the manner in which certain accounting transactions are recorded by DeCA.

For example, one system does not contain a general ledger account to record unexpended appropriation transfers. As a result, DeCA and its Defense Finance and Accounting Service (DFAS) – Columbus Center and DeCA personnel must use a combination of information inside and outside of that system to calculate unexpended appropriation transfers at the end of each reporting period. Also, neither system is able to process transactions in accordance with the USSGL at the detail level, resulting in the need to apply extensive manual processes to adjust balances in those systems prior to DeCA preparing its financial statements.

In addition, DeCA has to record many accounting transactions outside its general ledger and related sub-accounting system modules throughout the year, resulting in a high volume of manual journal vouchers (JVs) being prepared prior to the compilation of its financial statements. Specifically, in connection with its preparation of its financial statements for the quarter ended June 30, 2018, DeCA prepared 160 JVs to a variety of accounts with an absolute value of approximately \$13 billion. Many of these entries are necessary as a direct result of the noncompliance and limitations of the systems.

DeCA's inventory accounts also require significant manual intervention to record a variety of accounting events, including allowances for losses relating to physical changes to inventory during the year. Through September 30, 2018, 41 inventory-related JVs were processed with an absolute value of \$1.2 billion. The volume and complexity of the JVs processed in the inventory general ledger accounts increases the risk that the composition of the inventory value (cost, shrinkage and valuation adjustments) at year end is incorrectly reported in DeCA's financial statements.

System limitations have also indirectly affected DeCA's recording of certain vendor transactions, resulting in inconsistent reporting of revenues and expenses by certain commissaries.

The Federal Financial Management Improvement Act of 1990 Section 803(a) requires that "each agency shall implement and maintain financial management systems that comply substantially with Federal financial management systems requirements...and the USSGL at the transaction level."

Chapter 9500 of the Treasury Financial Manual provides detailed guidance for evaluating compliance with the requirements of FFMIA.

Even though we found that the dollar impact of certain vendor transactions being recorded inconsistently was immaterial to the financial statements, JVs (including those for inventory) processed during the year were materially correct, and DeCA has compensating controls to monitor the use of these JVs, these procedures are inefficient and the risk of error in DeCA's financial statements during the year is increased by these manual entries.

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT B (Continued)

Recommendations:

We continue to recommend that DeCA:

1. Ensure the design of the business processes and data structure of the new systems to be implemented will meet DeCA's unique business needs, as well as federal system and accounting requirements.
2. Continue to monitor the volume and nature of manual journal entries (JVs) to ensure that JVs are only used for transactions that cannot be handled by the current accounting systems (including relevant modules).
3. Continue to employ compensating control procedures, through additional analytical processes and detailed reconciliations, to ensure period end financial statements are accurately presented.
4. Explore opportunities for all commissaries to report revenues and expenses to DeCA headquarters consistently prior to the new system implementation.

INDEPENDENT AUDITORS' REPORT (Continued)
EXHIBIT C
Status of Prior Year Findings

Prior Finding	Recommendation	Current Status
Financial Accounting Reporting and Analysis	<ol style="list-style-type: none"> 1. Monitor the volume and nature of manual JVs to ensure that JVs are only used for transactions that cannot be handled by the current accounting systems (including relevant modules). 2. Employ compensating control procedures, process and detailed reconciliations, and other analytical tools to review period end financial statements to ensure that amounts reported in the financial statements are accurately presented. 3. Explore opportunities for all commissaries to report revenues and expenses to DeCA headquarters consistently prior to the new system implementation. 	Finding merged with current year noncompliance finding
Systems' Noncompliance with the Federal Financial Management Improvement Act	<ol style="list-style-type: none"> 1. DeCA continue to work with DoD (including DFAS) to implement actions to replace its accounting systems to one that is fully integrated and in compliance with the requirements of FFMA. 	Repeat Finding

INDEPENDENT AUDITORS' REPORT (Continued)
Exhibit D
Management's Response to Auditors' Report



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

CCR

November 8, 2018

Mr. Roger Von Elm, Principal
CliftonLarsonAllen, LLP
901 N. Glebe Road, Suite 200
Arlington, VA 22203-1853

Mr. Von Elm:

In response to the Independent Auditors' Report dated October 2018, of the Fiscal Years 2018 and 2017 financial statements of the Defense Commissary Agency (DeCA), management generally agrees with all findings of this report. Specifically, DeCA provides the following comments related to the material weakness in Exhibit A Controls over Inventory Need Improvement, Exhibit B Noncompliance with the Federal Financial Management Systems Requirement and Exhibit C Status of Prior Year Findings of the report.

Exhibit A Controls over Inventory Need Improvement: DeCA is in a state of transformation, particularly as it relates to our resale operations. As defined in NDAA 17, DeCA introduced variable pricing and private label which in effect changed our business model to allow us to competitively price products while generating margin. In conjunction with this transformation in our business, we are deploying a new integrated commercial grocery inventory ordering and management system (known as EBS). This is a major shift from our cost plus one percent equals shelf price inventory where validation was based on percent of change from recorded book value. We are moving towards a full perpetual inventory where the count is by SKU and an inventory methodology where validation will be based on a threshold, to be defined, and a deviation of counts at specific product level. This change will be occurring over the next two years. During this time DeCA will be developing and implementing new accounting and business processes for full perpetual inventories at the stores and CDCs while taking into account the auditors findings and recommendations. In addition, newly defined processes for enabling perpetual validation at legacy stores will be used to perform formal cyclical counts at stores and adjust book values as required. This shift in methodology as documented in the 2018 audit opinion identifies inventory related areas that require improvement. As we work to improve our processes, it is our goal that DeCA will achieve an unmodified opinion in our post deployment environment.

As noted in **Exhibits B Noncompliance with Federal Financial Management Systems Requirement and Exhibit C Status of Prior Year Findings**, DeCA's financial management systems are not in compliance with the requirement to use U.S. Standard General Ledger (USSGL) at the transaction level as documented in the FFMIA of 1996. DeCA acknowledges this non-compliance resulting from the use of aging and outdated technology from two key legacy systems, the Defense Business Management System (DBMS) and the Standard Finance System (STANFINS). DeCA is currently in the process of deploying a new resale system that will feed into the Defense Agency Initiative (DAI) at the same point that DAI is deployed for our

Your Commissary ... It's Worth the Trip!

INDEPENDENT AUDITORS' REPORT (Continued)
Exhibit D
Management's Response to Auditors' Report

non-resale (Commissary Operations and Surcharge) accounts, slated for FY 2021. This integration into DAI is the corrective action plan for these repeat findings.

In the interim, the need to combine information from two legacy systems for consolidated reporting creates the need for a higher than normal level of manually processed journal vouchers (JVs) to ensure accurate reporting. DeCA has numerous compensating controls in place to include systems reconciliation, JV reviews, JV approvals and USSGL crosswalks to ensure accurate financial reporting. DeCA works closely with our service provider, DFAS, to employ controls on their end of the JV process to ensure accuracy, nature and necessity.

If there are additional concerns regarding these responses, please address those to me or Ms. Linda Randall, Director of Accounting. I can be reached at 804.734.8000, ext. 48794, Cynthia.morgan@deca.mil or Ms. Randall can be contacted at (804) 734- 8000 X 8642 or linda.randall@deca.mil.

MORGAN.CYNTHIA
A.L. 1229474231

Digitally signed by
MORGAN.CYNTHIA.L.12294742
31
Date: 2018.11.21 15:17:02 -0500

Cynthia L. Morgan
Chief Financial Officer
Defense Commissary Agency

This page intentionally left blank

Glossary of Acronyms

ACM	–	Asbestos Containing Material
ACSI	–	American Customer Satisfaction Index
AFR	–	Agency Financial Report
BSC	–	Balance Scorecard
BSF	–	Buildings, Structures, and Facilities
CCSS	–	Commissary Customer Service Survey
CDC	–	Central Distribution Center
CFI	–	Claes Fornell International
CFO	–	Chief Financial Officer
CLA	–	CliftonLarsonAllen
CPI	–	Continuous Process Improvement
CRA	–	Continuing Resolution Authority
CUEC	–	Complimentary User Entity Controls
CSRS	–	Civilian Service Retirement System
DeCA	–	Defense Commissary Agency
DFAS	–	Defense Finance and Accounting Service
DoD	–	Department of Defense
DOL	–	Department of Labor
DWCF	–	Defense Working Capital Fund
EBS	–	Enterprise Business Solution
EUI	–	Energy Use Intensity
FBWT	–	Fund Balance with Treasury
FASAB	–	Federal Accounting Standards Advisory Board
FCI	–	Facility Condition Index
FECA	–	Federal Employees Compensation Act

Glossary of Acronyms

FGLI	–	Federal Employees Group Life Insurance
FEHB	–	Federal Employee Health Benefits
FERS	–	Federal Employees Retirement System
FFMIA	–	Federal Financial Management Improvement Act of 1996
FMFIA	–	Federal Managers’ Financial Integrity Act
FY	–	Fiscal Year
GAAP	–	Generally Accepted Accounting Principles
GF	–	General Funds
GOTS	–	Government Off-the-Shelf
GPRAMA	–	Government Performance and Results Modernization Act
ICOFR	–	Internal Controls over Financial Reporting
ICOFS	–	Internal Controls over Financial Systems
ICONO	–	Internal Controls over Non-Financial Operations
IDEAS	–	Improve Defense Commissary Agency’s Efficiency and Service
KBTU	–	Kilo British Thermal Units
LAC	–	Latest Acquisition Cost
M&RA	–	Manpower and Reserve Affairs
MICP	–	Manager’s Internal Controls Program
MOU	–	Memorandum of Understanding
NDAA	–	National Defense Authorization Act
NESHAP	–	National Emission Standards for Hazardous Air Pollutants
OAS	–	Organizational Assessment Survey
OASD	–	Office of the Assistant Secretary of Defense
OMB	–	Office of Management and Budget
OPM	–	Office of Personnel Management
OSBP	–	Office of Small Business Programs
OWCP	–	Office of Worker’s Compensation Programs

Glossary of Acronyms

PAR	–	Performance and Accountability Report
MICP	–	Manager’s Internal Controls Program
POWER	–	Protecting Our Workers and Ensuring Reemployment
RCRA	–	Resource Conversation and Recovery Act
SAT	–	Senior Assessment Team
SB	–	Small Business
SBR	–	Statement of Budgetary Resources
SCNP	–	Statement of Changes in Net Position
SDB	–	Small Disadvantaged Business
SDVOSB	–	Service Disabled, Veteran-Owned, Small Business
SF	–	Square Feet
Treasury	–	United States Department of the Treasury
TGA	–	Treasury General Account
TSCA	–	Toxic Substance Control Act
US	–	United States
USMC	–	United States Marine Corps
USSGL	–	United States Standard General Ledger
WCF	–	Working Capital Fund
WOSB	–	Woman-Owned Small Business
WUI	–	Water Use Intensity