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Defense Primer: Defense Working Capital Funds

Since 1870, the U.S. military has used working capital funds to procure and provide materiel and commercial products and services to its forces. Authorized under 10 U.S.C. §2208, a Defense Working Capital Fund (DWCF) is a type of *revolving fund* that is intended to operate as a self-supporting entity to fund business-like activities (e.g., acquiring parts and supplies, equipment maintenance, transporting personnel, research and development) for the Department of Defense (DOD). DWCF transactions move hundreds of billions of dollars within DOD annually.

According to DOD Financial Management Regulation (FMR) 7000.14-R, *revolving fund* accounts finance a “continuing cycle of business-type operations” by incurring “obligations and expenditures that generate receipts.” DWCFs are designed to break even over the long term through fees charged for products and services provided. These funds are widely used across the DOD in an effort to provide continuous base-support services, utilities, and industrial capabilities.

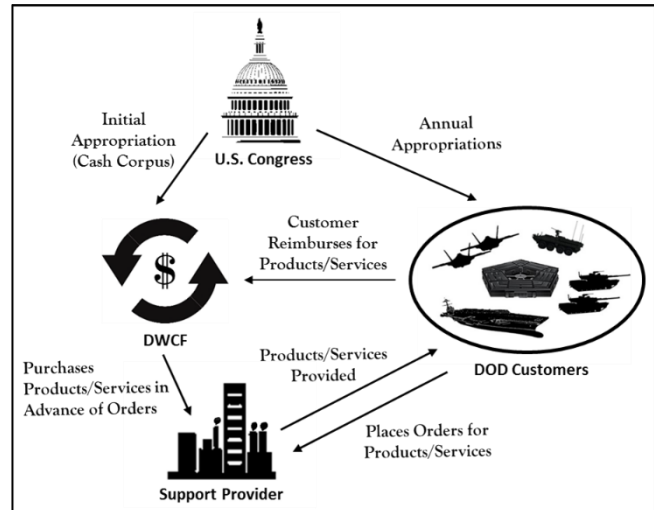
DWCFs offer benefits and flexibility to government procurement. They generally operate without fiscal year limitations (i.e., amounts in a DWCF account do not expire); they facilitate the aggregation of orders, allowing the government to leverage its purchasing power; and they allow for the establishment of product inventories that can reduce delivery time.

Fund Basics

When establishing a DWCF, Congress typically provides a direct appropriation to the fund. This initial appropriation and positive fund balance is called a *cash corpus*. Using the corpus, fund managers purchase products and services, usually in advance of an anticipated requirement (e.g., a depot overhaul of an aircraft platform), then establish a product catalog (e.g., an aircraft parts and supplies catalog) for its customers. Fund managers then set product prices and stabilized rates for services that typically do not change until the next fiscal year.

Once a DWCF-funded organization (e.g., a depot) is open for business, the customer—normally a military unit or DOD organization (though a private party can be a customer)—orders the product or service through a reimbursable agreement. Upon receipt of the product or service, the government customer then reimburses the DWCF with operation and maintenance funds appropriated for that specified purpose. If the customer is a private party, they typically prepay for products and services.

Figure 1. How a DWCF Operates



Source: CRS Graphics.

Notes: The process illustrated above is a general example of how a DWCF operates. Variations can exist (e.g., private party customers).

Rates and Budgeting

Fund managers typically establish rates 18-24 months ahead of schedule, locking in rates for the specified future fiscal year. DWCFs are expected to be self-sustaining after the initial appropriation. Fund managers establish rates taking into account *all costs* associated with each anticipated transaction, including the cost of the goods and services and a surcharge that includes overhead, operating, and administrative expenses.

DWCFs are typically organized by budget activity (i.e., a category within each fund that identifies the purposes, projects, or types of activities financed by the fund). In a supply-oriented budget activity fund, a surcharge is generally added to items provided in order to cover management and other overhead expenses such as shipping costs. For budget activities that are not supply-oriented (e.g., maintenance or information technology services), fund managers establish surcharge rates based on an estimated unit cost of the service provided plus overhead costs. In general, fund managers budget to recover all operating expenses including

- **direct costs**, such as labor and materials;
- **indirect costs**, such as facilities operation and maintenance;
- **hardware costs**, such as acquisition and repair of equipment needed to support operations;
- **operations costs**, such as labor, travel, training, transportation of personnel; and
- **other general and administrative costs**.

Financial Management

DWCFs may realize gains or losses within each fiscal year. At the end of the fiscal year, fund managers can recoup losses by establishing higher rates in future years, or if necessary, by seeking additional appropriations from Congress. Inversely, fund managers assess gains and lower rates for customers in future fiscal years, potentially providing a benefit to customers. Regardless, DWCFs must maintain a net positive cash balance at all times to avoid Anti-Deficiency Act (P.L. 97-258, 96 Stat. 923) violations.

DOD FMR 7000.14-R directs DWCFs to operate on a “break-even” basis (revenue generated equals the cost associated with receiving the revenue). Fund managers track and report two main types of operating results: the (1) *net operating result* (NOR), which is the net difference between expenses and funds received for a single fiscal year; and (2) *accumulated operating result* (AOR), which is the net difference between expenses and funds received since the inception of the fund. Managers normally examine AOR when establishing future rates for customers.

A Brief History of DWCFs

DWCFs were codified in law in 1962 in P.L. 87-651 §207(a) (10 U.S. Code § 2208), which provides the Secretary of Defense the authority to create a variety of working capital funds to support DOD operations.

In 1991, the Secretary of Defense combined five industrial funds, four stock funds, and multiple appropriated fund support activities established by the DOD and the services into what was titled the *Defense Business Operations Fund* (DBOF). This consolidated fund was created to streamline management and oversight responsibilities. Major activities performed under the DBOF included depot maintenance, transportation, supply management, and finance and accounting.

By 1996, DOD recognized the difficulty in managing one large DWCF, including the challenge of setting suitable rates for the entire DOD. As a result, the Under Secretary of Defense (Comptroller) disestablished the DBOF and reorganized it into three military department funds and one defense-wide fund. In 1997, a second defense-wide working capital fund (sometimes referred to as a DWCF) was established for the Defense Commissary Agency. Today, there are several defense-wide working capital funds.

Military Department DWCFs

Air Force Working Capital Fund (AFWCF)

The Deputy Assistant Secretary for Budget (SAF/FMB) manages the AFWCF. There are two activity groups in the fund: Consolidated Sustainment and Supply Management-Retail. SAF/FMB is also the Executive Agent for the Transportation Working Capital Fund (TWCF), however United States Transportation Command manages day-to-day operations of the TWCF.

Army Working Capital Funds (AWCF)

The Assistant Secretary of the Army (Financial Management and Comptroller) manages the AWCF. There

are two activity groups in the fund: Industrial Operations and Supply Management.

Navy Working Capital Funds (NWCF)

The Assistant Secretary of the Navy (Financial Management & Comptroller) manages the NWCF. Five activity groups within the fund support the Navy and Marine Corps: Depot Maintenance, Base Support, Supply Management, Research and Development (all Naval Warfare Centers and the Naval Research Laboratory), and Transportation.

Select Defense-Wide DWCFs

Defense Commissary Agency (DeCA)

The Under Secretary of Defense (Personnel and Readiness) has oversight of the DeCA DWCF. (See CRS InFocus IF11089, *Defense Primer: Military Commissaries and Exchanges*, by Kristy N. Kamarck and Barbara Salazar Torreón) There are two activity groups in the fund: Commissary Resale Stocks and Commissary Operations.

Defense Information Systems Agency (DISA)

The DOD Chief Information Officer oversees the DISA DWCF. There are two activity groups in the fund: Computing Services and Telecommunications/Enterprise Acquisition Services.

Defense Finance and Accounting Service (DFAS)

The Under Secretary of Defense (Comptroller) oversees the DFAS DWCF. DFAS is the one activity group within the fund.

Defense Logistics Agency (DLA)

The Assistant Secretary of Defense (Sustainment) has oversight of the DLA DWCF. There are three activity groups in the fund: Consumable Supply Management, Energy Management, and Document Automation and Production. DLA is also the Executive Agent of the DWCFs for DFAS and DISA.

Budget Information

Budget information for DWCFs is publicly available through the DOD Comptroller’s website. The annual budget justification books provide a financial profile of each fund over a three-year period (year of the request and two years prior). The profile generally includes an accounting of fund revenues, operating expenses, capital investments, cash forecasts for the budget year, and NORs and AORs (actual and projected).

The budget justification books also depict and explain any anticipated rate/surcharge adjustments, and provide details to support requests for direct appropriations when required. They may also provide information on fund operations to include: performance metrics, management challenges, new initiatives, and manpower trends.

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