

CHAPTER 8

FINANCIAL CONTROL OF LIABILITIES0801 GENERAL

080101 Purpose. This chapter sets forth the policy to be followed in accounting for liabilities.

080102 Overview

A. A DoD liability is an amount owed by the DoD for items received, services received, expenses incurred, assets acquired, construction performed (regardless of whether invoices have been received), and cash advances received but as yet unearned. Included are amounts owed for goods and services in the hands of prime contractors but which are owned by the DoD under the terms of the contract, and amounts owed under grants, pensions, awards, and other indebtedness not involving the furnishing of goods and services.

B. A contingent liability occurs when a condition, situation, or set of circumstances exists that may confirm the loss or impairment of an asset or the incurrence of a liability. Accrual and disclosure of contingencies varies depending on their probability of occurrence. Estimated losses shall be recorded in DoD financial systems and reported in Component financial statements if:

1. Information available before the financial statements are issued indicates that an asset probably has been impaired or a liability probably has been incurred as of the date of the financial statements.

2. The amount can be reasonably estimated.

C. For the purpose of federal credit programs, a contingent liability is a conditional commitment that may become an obligation because of a future event beyond the control of the DoD. Contingent liabilities include Defense Production Loan Guarantees.

0802 ACCOUNTING POLICY FOR LIABILITIES

080201 A liability has three essential characteristics.

A. It embodies a present obligation to others which will be settled by the probable future transfer or use of assets at one of the following:

1. A specified or determinable date.
2. At the time of a specific event.
3. On demand.

B. Because of equitable or legal responsibility, the DoD has little or no discretion to avoid future sacrifice.

C. The transaction or event giving rise to the duty and responsibility has already happened.

080202 Although liabilities rest generally on legal rights and duties, a legal claim is not a prerequisite for qualification as a liability if future cash or other transfer of assets in settlement is otherwise probable and estimable.

080203 Amounts recorded as liabilities shall be supported by sufficient documentation that establishes the basis for the claim against the DoD. Such documentation includes receiving reports, court decisions, and estimates of accrued liabilities for personnel services provided but for which payment is not made until the next scheduled payday.

080204 Liabilities shall be recorded initially in the designated accounts for the accounting period during which the transactions giving rise

to them occurred and removed in the period during which they are liquidated.

080205 Liabilities shall be recorded at amounts that reasonably represent the cost of the economic benefit to be used in settlement.

080206 Liabilities shall be recorded regardless of the availability of funds to be used in their liquidation.

080207 When liabilities are incurred as work is performed rather than when deliveries are made, appropriate accruals shall be made from performance reports for the affected accounting periods.

080208 When property is acquired under a lease-purchase agreement, the liability shall be recorded when the property is accepted.

080209 Amounts received from other accounting entities as unearned revenue shall be recorded as liabilities until performance occurs.

080210 Goods and services purchased under long-term contracts shall be recorded as a liability in the period in which the goods or services are received and accepted by the agency. The related asset or expense, as appropriate, shall be recorded at the same time as the liability. When goods and services are to be received over a period of time covering 2 or more accounting periods and payment is to be made upon completion of delivery, the liability shall be recorded as a noncurrent liability until completion of delivery. A noncurrent liability is one that will not be paid within 1 year of its incurrence.

080211 For financial reporting purposes, DoD Components shall compute the liability for property, plant, and equipment manufactured or constructed for them under long-term contracts on the basis of verified estimates of work completed (percentage-of-completion method) per contractor reports or invoices received during each account period, rather than on disbursements made. DoD Components shall use the contractor's requests for progress payments, certified by an authorized contact administrator, as the basis for recording the

liability. Appropriate liabilities for contract retainages, if any, shall be recorded as contract holdbacks. The appropriate work in process or construction in progress accounts shall be adjusted to reflect the value of work completed, as represented by approved progress payments accepted by the DoD Component.

080212 The annual leave liability shall be accrued.

080213 The liability for the DoD contribution to civilian retirement benefits earned shall be accrued. The amounts recorded in the applicable general ledger accounts shall be that portion of the liability that is to be paid by the appropriation current at the time the liability was incurred.

0803 UNBILLED LIABILITIES

080301 Open accounts payables require constant review to assure that they are valid liabilities. If an invoice has not been received for a liability that represents acceptable final performance on a contract or order, the procedures in paragraph 080302, below, may be implemented unless the contract or order is in litigation. When litigation is in effect, the liability shall remain on the accounts.

080302 When the invoice has not been received within 180 days from the date of acceptable final performance the following guidance shall be followed:

A. If the amount of the payable is less than \$100 and 90 days have lapsed since the initial documented request, the liability shall be written off and the related obligation cancelled and returned to the unobligated balance of the appropriation fund account.

B. If the amount of the payable is more than \$100 and there is documentation on file that at least 2 written requests have been made for an invoice, the liability shall be written off and the related obligation cancelled and returned to the unobligated balance of the appropriation fund account. To qualify for the write off and deobligation, the second request

for an invoice shall be dated at least 60 days before the date of the write off.

080303 Late invoices received must be matched against documentation of liabilities previously written off to determine their validity before payment. If a late billing is determined to be valid, the liability shall be reestablished and funds obligated and paid from an appropriate account (current appropriation or expired account). For expired accounts, the payment of a valid late bill shall be treated as an obligation adjustment. For cancelled accounts, the payment of a valid late bill should be from a current account (available for the same purpose as a canceled account), in an amount not to exceed the lesser of any remaining unobligated balance of the cancelled account or 1% of the current account. A portion of funds available for funding activity cost center will be reserved within each appropriation or fund for invoices received subsequent to writeoff.

080304 The funded amount maintained in the reserve for late bills shall be established at a level sufficient to preclude a violation of 31 U.S.C. 1341 or 1517(a) or both from receipt of valid late bills. The amount of the reserve for late bills shall be reviewed and approved by the comptroller of the activity annually, to determine if adjustment based upon experience is appropriate.

0804 ADJUSTING JOURNAL VOUCHERS

080401 The source documents used for accounts payable postings include receiving reports, invoices, and contractor reports, etc. As a general rule, all entries to the accounting system must be based upon routinely prepared source documents, which have been processed under prescribed internal control procedures. If source documents are not received, necessary follow up actions are taken to obtain the required documents. The unrecorded source document condition may have been caused by the failure to record a receiving report, or a particular transaction may have failed to post in an automated accounting system. Such events will be recorded on research listings as an unmatched item or a required document that has not been received. When the listings are

received, required research effort normally begins by first stratifying transaction by dollar values. Those in the highest category (over \$1 million, for example) will be researched first. When the first category is completed the next category (from \$100,000 to \$1 million, for example) will be researched until that group is completed. This operational review continues until all items have been resolved. Then the process is restarted when the next listing is received. Management is expected to monitor constantly the volume and dollar values of transactions requiring research and to authorize overtime, details of personnel, etc., when necessary, to assure required research is completed. However, there are competing requirements that can result in a significant value of low dollar transactions which have not been researched for long periods of time. Further, as a practical matter, it is not always cost effective or realistic to expend the effort necessary to obtain each and every source document. When this occurs, management may decide to process adjusting journal vouchers using the process described in this section.

080402 The need for an accounting adjustment is properly a decision to be made at the level at which an account is maintained. The decision, however, must be supported by documentation that shows reasonable and prudent research was conducted to support the adjustment. This document then must be retained for audit.

080403 Normally, the first step in the adjustment process is to group unmatched items into homogeneous lots. Each of these lots is then subjected to acceptance sampling. The sampling plan should follow normal statistical sampling procedures. If analysis of the sampled items confirms that there are unposted source documents for the entire lot, then applicable journal vouchers should be processed. If the sample discloses that some payables are invalid, or that some invoices have not been received, then estimation statistical sampling procedures should be applied to determine if research will cost more than likely recoveries. If statistical sampling procedures do not support either of the above actions, then each item in the lot must be subjected to normal research.