

CHAPTER 9**LIABILITIES**0901 GENERAL STANDARDS

090101. General Information. Additional information relating to liabilities may be found in [Volume 4](#), [Chapters 8, 9, 10, 12 and 13](#), of this Regulation.

090102. Definition

A. A liability for federal accounting purposes, is a probable and measurable future outflow or other sacrifice of resources as a result of past transactions or events.

B. The existence of a past event of financial consequence is essential for liability recognition. A transaction involves the transfer of something of value. Transactions may be either exchange transactions or nonexchange transactions. An exchange transaction arises when each party to the transaction sacrifices value and receives value in return. The Defense Working Capital Funds (DWCF) transactions are, nearly exclusively, exchange transactions. A nonexchange transaction arises when one party to a transaction receives value without directly giving or promising value in return. The word “probable” as used in the above definition refers to that which can reasonably be expected or is believed to be likely to occur on the basis of available evidence or logic and is assessed on the basis of current facts and circumstances. “Measurable” means that an item has a relevant attribute that can be quantified in monetary units with sufficient reliability to be reasonably estimable.

★ C. Characteristics of a Liability. A liability has three essential characteristics:

1. It embodies a present duty or responsibility to one of more other entities that entails settlement by probable future transfer or use of assets at a specified or determinable date, on occurrence of a specified event, or on demand,

2. The duty or responsibility obligates a particular entity, leaving it little or not discretion to avoid the future sacrifice, and,

3. The transaction or other event obligating the entity has already happened.

090103. Recognition of Liabilities

A. A liability should be recognized when it is incurred, regardless of whether it is covered by available budgetary resources. Financial statement disclosure should be made for liabilities that are not covered by available budgetary resources.

B. 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.

090104. Contingent Liabilities. A contingency is an existing condition, situation, or set of circumstances involving uncertainty as to possible gain or loss to an entity. The uncertainty will ultimately be resolved when one or more future events occur or fail to occur. A contingent liability should be recognized in the DWCF financial reports and statements when all of these three conditions are met:

A. A past event or exchange transaction has occurred (e.g., a DWCF entity has breached a contract with a nonfederal entity).

B. A future outflow or other sacrifice of resources is probable (e.g., the nonfederal entity has filed a legal claim against a DWCF entity for breach of contract and the DWCF entity's management believes the claim is likely to be settled in favor of the claimant).

C. The future outflow or sacrifice of resources is measurable (e.g., the DWCF entity's management determines an estimated settlement amount). The estimated liability may be a specific amount or a range of amounts. If some amount within the range is a better estimate than any other amount within the range, that amount is recognized. If no amount within the range is a better estimate than any other amount, the minimum amount in the range is recognized and the range and a description of the nature of the contingency should be disclosed.

D. If none of the above three conditions are met, the contingent liability need not be disclosed in the DWCF financial reports and statements but should, nevertheless, be disclosed in notes regarded as an integral part of those reports and statements if there is at least a reasonable possibility that a loss or an additional loss may have been incurred. The probability classifications are probable (likely to occur); reasonably possible (more than remote but less than probable); and remote (chance of occurrence is slight).

090105. Capital Lease Liabilities. Capital leases are leases that transfer substantially all the benefits and risks of ownership to the lessee. Additional information relating to capital leases may be found in [Volume 4, Chapters 6](#), "Property, Plant, and Equipment," of this Regulation. If, at its inception, a lease meets one or more of the following four criteria, the lease should be classified as a capital lease by the lessee:

A. The lease transfers ownership of the property to the lessee by, or at, the end of the lease term.

B. The lease contains an option to purchase the leased property at a bargain price.

C. The lease term is equal to, or greater than, 75 percent of the estimated economic life of the leased property. (This criteria is not applicable when the beginning of the

lease term falls within the last 25 percent of the total estimated economic life of the leased property.)

D. The present value of rental and other minimum lease payments, excluding that portion representing executory cost to be paid to the lessor, equals or exceeds 90 percent of the fair value of the leased property. (This criteria is not applicable when the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property.)

090106. If a lease does not meet one of the above four criteria, it should be classified as an operating lease. Operating leases are leases in which the entity does not assume the risks of ownership. Multi-year service contracts and multi-year purchase contracts for expendable commodities are not capital leases.

090107. The amount to be recorded by the lessee as a liability under a capital lease is the present value of the rental and other minimum lease payments during the lease term, excluding that portion of the payments representing executory cost to be paid to the lessor. The cost of general property, plant, and equipment acquired under a capital lease shall be equal to the amount recognized as a liability for the capital lease at its inception. During the lease term, each minimum lease payment should be allocated between a reduction of the obligation and interest expense so as to produce a constant periodic rate of interest on the remaining balance of the liability.

090108. Liabilities Covered by Budgetary Resources (Funded Liabilities). These are liabilities incurred which will be covered by available budgetary resources. Budgetary resources include: (a) new budget authority, (b) offsetting collections credited to an appropriation or fund account, (c) recoveries of unexpired budget authority through downward adjustments of prior year obligations, and (d) unobligated balances of such resources at the beginning of the year or transferred in during the year.

A. Federal Funded Liabilities. Federal liabilities, for the DWCF, are claims against the DWCF by non-DWCF and other federal entities. Federal liabilities include accounts payable to non-DWCF and other federal entities and other current liabilities such as advances and prepayments received from those entities.

B. Nonfederal Funded Liabilities. Nonfederal liabilities, for the DWCF as well as for other Department of Defense (DoD) entities, are amounts that the federal government or an entity within the federal government owes to nonfederal entities. The term “nonfederal entities” encompasses domestic and foreign persons and organizations outside the United States (U.S.) Government. The term “public” is also used to represent nonfederal entities. Nonfederal liabilities include accounts and interest payable to nonfederal entities, other liabilities due to nonfederal entities, and advances and prepayments received from nonfederal entities.

090109. Liabilities Not Covered by Budgetary Resources (Unfunded Liabilities). These are liabilities incurred which are not covered by available budgetary resources. These include liabilities resulting from the receipt of goods or services in the current or prior periods,

or the occurrence of eligible events in the current or prior periods, for which revenues or other sources of funds necessary to pay the liabilities have not been made available through congressional appropriations or earnings of the entity. Notwithstanding an expectation that the appropriations will be made, whether they in fact will be made is completely at the discretion of the Congress.

A. Federal Unfunded Liabilities. These are liabilities, not covered by available budgetary resources, that arise from transactions among federal entities.

B. Nonfederal Unfunded Liabilities. These are liabilities, not covered by available budgetary resources, that arise from transactions with nonfederal entities.

0902 SPECIFIC STANDARDS

090201. Accounts Payable. Accounts payable is amounts owed by a federal entity for goods and services received from, progress in contract performance made by, and rents due to other entities. Accounts payable are not intended to include liabilities related to on-going continuous expenses such as employees' salary and benefits, which are covered by other current liabilities. Amounts owed for goods or services received from federal entities represent intragovernmental transactions and should be reported separately from amounts owed to the public.

090202. Recognition of Accounts Payable. When an entity accepts title to goods, whether the goods are delivered or in transit, the entity should recognize a liability for the unpaid amount of the goods. If invoices for those goods are not available when financial statements are prepared, the amounts owed should be estimated. When a contractor provides the government with goods that are also suitable for sale to others, the liability usually arises when the contractor physically delivers the goods and the government receives them and takes formal title. When a contractor builds or manufactures facilities or equipment to the government's specifications, formal acceptance of the products by the government is not the determining factor for accounting recognition. Constructive or de facto receipt for facilities or equipment constructed or manufactured according to agreements or contract specifications occurs in each accounting period based on an estimate of work completed under the contract or agreement. The estimate of such amounts should be based primarily on the federal entity's engineering and management evaluation of actual performance progress and incurred costs. As a rule, actual performance progress and incurred costs are evidenced by progress billings from the contractor and are verified by the contract administrator.

090203. Interest Payable. Interest payable should be recorded for the amount of interest expense incurred and unpaid. Within the DoD, interest payable results primarily from late payment of bills by a DoD activity (see provisions in 31 U.S.Code (U.S.C.), 3901 through 3907, Prompt Payment) and on refunds (see provisions in 26 U.S.C. 6611). The provisions of the Prompt Payment Act require that interest penalties be paid from funds available to carry out the programs for which the penalty was incurred, that is, interest penalties under the Prompt Payment Act shall be charged directly to the account that funds the payment of the underlying liability.

090204. Other Current Liabilities. The term “other current liabilities” should be used to report current liabilities only when the liability cannot be recognized and reported in some specific categories such as accounts payable; interest payable; debt owed to the public, Treasury, or other entities; and liabilities for loan guarantee losses. Other current liabilities due to federal entities are intragovernmental liabilities that should be reported separately from those due to employees and the public. Other current liabilities include unpaid expenses that are accrued for the fiscal year for which the financial statements are prepared and are expected to be paid within the fiscal year following the reporting date. The DWCF activities are required to explain amounts recorded as other current liabilities that exceed the thresholds specified in [Volume 6B](#), of this Regulation. Examples of other current liabilities are:

A. Accrued employees wages, bonuses, and salaries for services rendered in the current fiscal year for which paychecks will be issued in the following year. The estimated accrual shall be recorded in the current accounting period, with reversing entries recorded after closing to avoid overstating liabilities in the following accounting period.

B. Advances and prepayments received for goods to be delivered or services to be performed. An advance equal to the price of an item shall be collected before delivery or shipment of an item to customer who is not chartered, sanctioned, authorized, or under contract to perform a function of the federal government. The federal government nonappropriated fund instrumentalities are authorized to perform a morale, welfare, and recreation function for the federal government. Before revenues are earned, the current portion of the advances and prepayments should be recorded as other current liabilities. After the revenue is earned (goods or services are delivered, or performance progress is made according to engineering evaluations), the entity should record the appropriate amount as a revenue or financing source and should reduce the liability accordingly.

090205. Relationship of Liabilities to Obligations. A federal entity, under budgetary accounting, records an obligation (i.e., an undelivered order) when the entity places a purchase order or signs a contract. An obligation, once incurred, reduces an entity’s resources available for obligation. Budgetary accounting entries are required to record the amounts obligated and to reduce the available budget authority. For financial reporting purposes, liabilities are recognized when goods and services are received or are recognized based on an estimate of work completed under a contract or agreement. When liabilities are recognized, the undelivered order recorded in budgetary accounts is reduced and an accrued expenditure-unpaid is recorded.

090206. Supporting Records. Supporting records shall be maintained for all liabilities. The supporting record shall identify the amount owed by individual transaction, the date recorded, and the identity of the payee. At least quarterly, the supporting records shall be reconciled with the general ledger balance. All differences shall be investigated and all errors corrected.