Chapter 17
Appendices

Appendix E: Accruals, Estimates and Undelivered Orders

MEMORANDUM

To: Heads of Bureaus
Chief Financial Officers
Departmental Offices
Bureau Finance Officers

From: Nina Rose Hatfield
Deputy Assistant Secretary, Budget and Finance

SUBJECT: Accruals, Estimates and Undelivered Orders

In the Fiscal year 2002 Department of Interior (DOI) Consolidated Audit, KPMG included controls over undelivered orders and accruals as reportable conditions. KPMG identified that DOI has not fully implemented internal controls to ensure that obligations are liquidated and liabilities are accrued for goods and services received prior to the end of the reporting period. In addition, KPMG stated that DOI does not de-obligate funds in a timely manner.

KPMG made the following recommendations:

1. Develop and communicate internal controls to ensure that accruals are recorded and undelivered orders are adjusted for services and products received prior to the end of the reporting period.
2. Implement internal controls to ensure that the accruals and undelivered orders that are recorded are properly supported. These procedures should be completed at least quarterly.

The Department established an Accruals Team with representatives from six bureaus, to develop policies for undelivered orders, accruals and estimates together with personnel from KPMG and Office of Inspector General. Attached are the undelivered orders policy and the accruals and estimates policy. These documents are a starting point that begins to address KPMG's recommendations. We will not eliminate the reportable condition until we have successfully implemented these policies. The policies are effective as of the date of this memorandum and will also be issued as an appendix to the financial statement guidance.

If you have any questions concerning these documents, please call Debra Carey at (202) 208-5542.

cc: Finance Officers Partnership
Financial Statement Guidance Team

DEPARTMENT OF THE INTERIOR

POLICY FOR UNDELIVERED ORDERS

I. PURPOSE

This document establishes the Department of Interior (DOI) policy for review of undelivered orders.

II. AUTHORITIES

The "Antideficiency Act," 31 USC 1341, 1349-1351, 1501-1557.

III. RESPONSIBILITIES

Assistant Secretaries, Bureau Directors, bureau financial officials, and program managers are responsible for implementing proper procedures to ensure the timely review of undelivered orders, cancellation of invalid undelivered orders, and certification of valid undelivered orders.

IV. EFFECTIVE DATE

This policy is effective upon issuance.

V. DEFINITION OF UNDELIVERED ORDER

Contracts or orders issued by the ordering activity for goods or services that have not been received. No expense or accounts payable should be incurred for undelivered orders.

VI. REASONS FOR REVIEW OF UNDELIVERED ORDERS

The timely expenditure of obligated funds is a fundamental principle of sound financial management. Excess undelivered orders serve as an indicator that a manager may not be effectively using allocated funds. Recurring reviews of undelivered orders, resulting in cancellation or deobligation of invalid obligations, increases funds available for no-year appropriations and for annual appropriations if the obligation to the annual fund occurred in the current fiscal year.

VII. MIMIMUM REVIEW REQUIREMENTS

A. Review undelivered orders quarterly.
B. Document and certify quarterly all undelivered orders over 12 months old with no activity, indicating why the obligation is valid. If the obligation is invalid, deobligate

the obligation with appropriate supporting documentation. Retain the quarterly documented review for reference and audit.

C. Review current year annual obligations as appropriate to identify invalid obligations.
D. Include any adjustments prior to the end of the reporting period, quarterly or annually.
E. Complete the documented, certified quarterly review 30 days after the end of the quarter.

Report the completed review as a key performance measure accomplishment to the Office of Financial Management (PFM) as required by the performance measure reporting requirements.

ACCRUAL ACCOUNTING POLICY

I. PURPOSE:

This document sets forth basic principles, requirements and techniques for Department of Interior (DOI) accounting on an accrual basis, whereby financial transactions are recorded in the period of occurrence, even though related cash is disbursed or received during another period. Use of the accrual method provides DOI management with financial performance information so that informed decisions may be made.

II. AUTHORITY:

31 USC 3512(e)

III. RESPONSIBILITIES:

Assistant Secretaries, Bureau Directors, bureau financial officials, and program managers are responsible for implementing proper procedures and ensuring reliable accruals, including approving accruals developed by personnel outside the finance offices.

IV. EFFECTIVE DATE:

This policy is effective upon issuance.

V. POLICY

DOI Bureaus/Departmental Offices must develop an accrual (estimation) methodology that provides valid, timely financial estimates. Bureau-specific processes and policies must meet Generally Accepted Accounting Principles (GAAP) and be supportable. Bureaus/Departmental Offices must determine the estimation methodology for all types of accruals, document and test the methodology, obtain concurrence from the financial statement auditors for the methodology, and forward the documentation to DOI Office of Financial Management by June 1 of each year. Documentation reflecting computation and support for accruals and analysis of accuracy of accruals shall be retained for reference and audit.

DOI Bureaus/Departmental Offices must compute accruals and record them in the accounting system for each quarterly accounting period. The accruals must be entered into the accounting system prior to quarter-end and September 30 annually.

VI. DEFINITION OF ACCRUALS (ESTIMATES)

The accrual method of accounting recognizes the significance and accounting aspects of financial transactions, events, or allocations in the reporting periods they occur. Costs are recognized in the accounts when incurred and revenues are recognized when they are earned.

VII. CRITERIA FOR DEVELOPING ESTIMATES

All Bureau/Departmental Office estimation processes must consist of the following steps—

A. Identify situations for which accounting estimates are required.
B. Identify and document the relevant factors that may affect the accounting estimate. This includes subjective as well as objective factors. The factors should be based on management's knowledge and experience about past and current events and its assumptions about conditions it expects to exist and courses of action it expects to take.
C. Accumulate relevant, sufficient, and reliable data on which to base the estimate. Define data elements key to the methodology. Assess the validity of historical data.
D. Develop and document assumptions that represent management's judgment of the most likely circumstances and events with respect to the relevant factors (including any exceptions).
E. Determine the estimated amount based on the assumptions and other relevant factors. Demonstrate that the aggregate values below any established threshold or accounts not considered are insignificant.
F. Determine that the accounting estimate is presented in conformity with applicable accounting principles and that disclosure is adequate.
G. Consider whether the resulting accounting estimate is consistent with the operational plans of the entity.
H. Compare prior accounting estimates with subsequent results to assess the reliability of the process used to develop estimates.
I. Establish internal controls over the estimation process including review and approval by management (someone other than the preparer) of the accounting estimates, including—
    1. Sources of relevant factors
    2. Development of assumptions
    3. Reasonableness of assumptions and resulting estimates
    4. Consideration of the need to use the work of specialists
    5. Consideration of changes in previously established methods to arrive at accounting estimates

VIII. CATEGORIES FOR WHICH ESTIMATES MAY BE DEVELOPED

Estimates may be developed for the following categories.

A. Personnel Compensation, Personnel Benefits and Related Payments

- Gross compensation, including overtime, will be accrued through the end of each quarter. A labor distribution system may be used to distribute actual charges to cost accounts and to credit accounts payable. If the labor distribution to cost accounts does not vary significantly from payroll period to payroll period, the cost distribution of a representative preceding payroll or the total annual payroll to date may be used in determining the current accrual.
- Merit bonuses and awards, if significant in amount, will be accrued in the quarter earned.
- The cost of unused annual leave, compensatory time and credit hours earned will be accrued quarterly. Obtain accrued annual leave amounts from the Federal Personnel and Payroll System.
- Benefits, including benefits to Social Security, retirement funds, the Thrift Savings Plan, and group health and life insurance programs will be accrued in the same manner as gross compensation. Other benefits, such as relocation-related real estate costs and personnel allowances, shall be accrued in the quarter earned.
- Payments to the Office of Personnel Management for reemployed annuitants and severance pay for former employees will be accrued in the same manner as gross compensation.
- Recruitment and relocation bonuses and retention allowances shall be accrued in the quarter earned.

B. Travel and Transportation

- Transportation, perdiem, and miscellaneous costs are obligated when the travel is vouchered or travel card billing received from Bank of America. At the end of the quarter and yearend, the travel accrual is based on unvouchered travel information obtained from Bureaus and Departmental Offices, if significant.
- Permanent change of station travel, transportation costs, and transportation of household goods are accrued when incurred.

C. OPM Life Insurance, Health Insurance, FERS Retirement, and CSRS Retirement, and DOL Unemployment Compensation, Workers' Compensation

- Establish a quarterly amount in quarter 01. Review and adjust accrual amount as needed. DOI, Office of Financial Management will provide yearend accrual amounts from OPM and DOL.

D. Intra-departmental transactions

- Accruals for intra-departmental transactions will be posted in conjunction with the elimination reconciliation process or from supportable estimates. Any accruals should be booked prior to the elimination process. Billings for current costs will be billed according to the OMB Business Rules.

E. Depreciation of Capitalized Real and Personal Property

- Depreciation will be computed and recognized on a monthly basis. Refer to DOI Real Property Financial Management Policy, Item X – Depreciation for real property procedures.

F. Contingent Liabilities

- Record contingent liabilities based on reports from the Solicitor's Office which indicate a loss that is probable and can be reasonably estimated.

G. Environmental Liability

- Quarterly estimate is based on data provided by field offices.

H. Interest on Investments

- Interest on investments is entered the last day of the quarter based on Bureau and Treasury data.

I. Accounts Receivable and Allowance for Doubtful Accounts

- Accounts receivable and allowance for doubtful accounts are recorded quarterly.

J. Charge Card Purchases

- Charge card purchases billed from Bank of America through month end or yearend are processed as current period business. Any significant amounts not billed by Bank of America are included as estimates.

K. Miscellaneous Revenue, including non-DOI reimbursements

- Revenue shall be accrued in the quarter in which it is earned.
- Include unbilled receivables and accruals for non-DOI agencies and the public.

L. Contracts, Purchase Orders, and Cooperative Agreements

- See Item IX, "Accrual Methodology for Accounts Payable" below

M. Grants

- Bureaus/Departmental Offices may use historical or actual data.

N. Inventory and Inventory Allowance

- If a Bureau employs a perpetual inventory system, make a rational allowance for excess, obsolete, or unserviceable inventory on a quarterly basis. If a Bureau accounts for inventory on other than a perpetual basis, determine the actual inventory at a point in time, and otherwise estimate both inventory and an allowance on a quarterly basis.

O. Revenues

When estimating payables to accrue, Bureaus must also take into consideration those payables related to reimbursable agreements.
The accrual methodology must be able to identify those transactions related to reimbursable agreements, and make the appropriate general ledger entries, as shown below.

131D Accounts Receivable-On Budget-Unbilled
    5200 Revenue From Services Provided
4251 Reimbursements Earned-Receivable
    4221 Unfilled Customer Orders W/O Advance
570A Appropriations Used-Operational Expenses
    3107 Unexpended Appropriations Used

IX. ACCRUAL METHODOLOGY FOR ACCOUNTS PAYABLE

A proposed "general approach" methodology for developing accounts payable estimates (accruals) for contracts, purchase orders, and cooperative agreements based on the use of historical data follows. This approach is not a "one size fits all approach".

A. Background

Calculating the amount of accrued expenses that should be included on the quarterly financial statements is currently a manual process. The process requires extensive input from the program offices and consumes much of the Finance Office's resources during the critical period of quarter/year-end document processing. To alleviate this labor-intensive process, this proposed methodology provides an estimation process for accounts payable that centralizes and automates the accrual process.

B. General Assumptions for Accounts Payable Accruals

In order for any accrual methodology to be successful, some general assumptions must be made. Bureaus and Departmental Offices may add or delete assumptions, use more historical data, etc. Support all assumptions by a detailed analysis that is reviewed and approved by management and supported by appropriate documentation. In accordance with the auditing standards, the financial statement auditors will request an analysis that supports each assumption below and subject this analysis to testing.

All Bureaus/Departmental Offices will list the assumptions that will be consistent throughout their process, such as:

- Bureaus/Departmental Offices may include intradepartmental accruals using this methodology if the results are supportable estimates. The accruals should be booked prior to the elimination process.
- All direct charges are cyclical; therefore, a cumulative average will be used to estimate the accrual for such transactions.
- All inter-governmental transactions occurring in a said month are for goods/services received during the preceding month. This presumes that the

OMB rules for intra-governmental transactions are implemented.
- Travel claims for temporary duty travel will be accrued if significant.
- All payments for utilities made during a month are for services received during the previous month.
- For all document types requiring a period of performance be entered into ABACIS, the dates entered are obtained from either the invoice or the receiving report.
- For all document types, the Invoice Date recorded in ABACIS/FFS reflects the actual date of the invoice.
- Past accrual history is representative of the current amount. However, if history does not prove consistency then the estimation process needs to be modified to consider the fluctuations of history and the current period.
- All accrual figures produced from this methodology are inclusive of only non-labor goods and services. The accrued payroll and benefits will continue to be based on the automated process.
- For all document types, the acceptance date in FFS is the received date. Consider that the vast majority of the goods or services with an acceptance period within two weeks of the end of the period are for goods or services provided in the previous period. Since there may be a number of days between receipt of the goods/services and the acceptance date entered into the accounting system, Bureaus using the acceptance date assumption should take a sample of payments and calculate the average number of days between when the goods/services were received and the acceptance date for the goods/services based on supporting documentation. To calculate the accrual, use the acceptance date less the average number of days between the receipt and acceptance dates to determine a representative receipt date. Update this analysis on a periodic basis.
- Undelivered orders are valid.

C. Proposed Accrual Methodology for Accounts Payables:

The proposed accrual methodology develops accruals by using quarterly historical data for the prior two fiscal years plus current fiscal year quarters. Two types of historical data are used: unliquidated obligations and invoices paid. Invoices with a receipt date for FFS or an end date for period of performance for ABACIS from the entire period are analyzed to determine what should have been accrued. For example, if you are evaluating the September 30, 2001 accrual on March 31, 2003, consider amounts paid through March 31, 2003**.** An accrual percentage is calculated comparing the amount of invoices that should have been accrued to the unliquidated obligations for the quarter. These accrual percentages are averaged for each comparable period (e.g. quarter l, 2001 and quarter l, 2002) to develop the percentage by document type to apply against the current quarter unliquidated obligations.

Direct charges may be accrued based on a cumulative average. Total direct charges are divided by the months analyzed. An example is: total direct charges for a fiscal year are $120,000. This equates to $10,000 per month.

The Bureau/Departmental Office can develop the accruals at the lowest cost level within the unliquidated obligation file. The automated accrual process is based on document types and their relative percentage to unliquidated obligations. Historical payment and unliquidated obligations data will be used to calculate the relative percentages to be used in the current year. Data analysis will continue to be evaluated throughout the current fiscal year to ensure that the estimated accrual amount is reasonable.

D. Payment Document Types

There are two general types of payment documents, those for direct charges (generally non-referenced documents) and those that are applied against an outstanding obligation. The method of entry into the accounting system determines whether the document is a "direct charge" document or is a payment against an outstanding obligation. The amounts of these document types must be further analyzed during the accrual process to ensure that the accrual amounts are accurate.

Document types that may be used in payment of direct charges may be accrued based on the cumulative average:

payments of FedEx, UPS, utilities, telephone bills, fire equipment rentals and blanket purchase agreement (BPA).

Document types that may be used in payment against an outstanding obligation may be accrued on the relative percentage basis:

payments of purchase orders and contracts where a purchase order/delivery order has been issued, cooperative agreements, non-DOI governmental transactions.

E. Calculating the Estimated Accrual for Obligated Documents

1. Download the historical payment UDO and payment data by fiscal year for the previous two fiscal years and the current fiscal year quarters to capture Bureau-specific data. Subtotal by quarter, document type, and capitalized vs. non-capitalized object classes. The reason for using historical data no older than the previous two fiscal years is because undelivered order data prior to fiscal year 2001 is not readily available**.**

2. Determine the Actual Accrual Amount
   In order to calculate the relative percentage to be applied to the current fiscal year's quarterly unliquidated obligated balance, the actual amount that should have been accrued in prior years must first be calculated.

   For each quarter involved in the historical data analysis, all payments made against the outstanding obligated balances must be obtained. This will identify the amount that should have been accrued had the actual figures been available at the time of the accrual estimate. Since the previous two fiscal years (2001 and

2002) are being included in the historical data analysis, each quarter will be analyzed separately. For example, when analyzing the first quarter of FY2001, all payments scheduled for payment after 12/31/00, which is the closing date of the accounting period under review, for a good/service that was received/performed during the first quarter will be calculated. The Receipt Date in FFS and the end date of the period of performance in ABACIS will be the date used to calculate this amount. Because the analysis is being performed 2 years after the fact, the actual amount that should have been accrued is now identifiable.

Perform the analysis on each quarter. The amount determined that should have been accrued will be used in the relative percentage calculation.

This data analysis will continue through the current fiscal year and any adjustments to the actual amount that should have been accrued in previous accounting periods will be made to ensure that the relative percentage calculation reflects actual historical data.

3. Determine the Unliquidated Obligated Balance

The Total Unliquidated Balance must be calculated for each period under analysis. This total will be used in calculating the relative percentage.

4. Calculate the Relative Percentage

To calculate the relative percentage for each document type, divide the total amount that should have been accrued (actual amounts paid after the close of the accounting period under analysis through the current accounting data available) for that payment document type by the total unliquidated balance for that obligating document type.

For example: The following chart contains all obligating document types appearing on the Unliquidated Obligations (UDO) Report for the period ending September 30, 2002 along with the total UDO balance for each document type (in column 1) as of September 30, 2002.

Calculation of Relative Percentage for the Period ending September 30, 2002 (Based on data through 2/28/03)

TA doc is excluded from analysis

Col 1	Col 2	Col 3	Col 4	Col 5
Oblig Documents	FY02 UDO Balance as of 9/30/02	UDO Sub-Totals	Total of Pmnt Docs made After 9/30/02	Year-End Accrual Percentage (Col 4/Col 3)
Contracts	41,550,809.24	41,550,809.24	4,367,545.47	10.5113%
GPO	48,029.99	48,029.99		
Purch Orders	223,717,206.72	223,717,206.72	46,673,531.27	20.8627%
Inter-agency Agreements	3,556,157.25			
Training	55,828.60			
GSA Work Orders	654,338.82	4,266,324.67	1,122,262.08	26.3051%
Relocation	1,558,499.63	1,558,499.63	124,855.51	8.0113%
Travel	(3,579.90)	(3,579.90)	64,003.13	
	271,137,290.35			

The chart also contains the actual amounts paid on these obligations between the periods of September 30, 2002 through February 28, 2003, that had a receipt date less than September 30, 2002 (which is the latest data available). This amount is what should have been accrued.

To calculate the relative percentage, divide the amount of the payment documents (Column 4) by the amount appearing in the UDO report for that document type (Column 3).

This percentage should be calculated for each historical period under analysis and the average of the percentages should be applied to the current UDO balances to calculate the estimated accrual for obligated documents. The percentage will be applied consistently to each document type having an outstanding unliquidated balance.

To calculate the relative percentage, divide the total amount that should have been accrued (actual amounts paid after the close of the accounting period under analysis) by the total unliquidated balance. Summarize obligations and payments to develop the relative percentage to support the entry.

F. **Calculating the Estimated Accrual for Direct Charge Documents**

Direct charges may be accrued based on a cumulative average. Total direct charges are divided by the quarters analyzed. An example is: total direct charges for a fiscal year are $120,000. This equates to $10,000 per month. The Bureau/Departmental Office can develop the accruals at the lowest cost level within the unliquidated obligation file.

G. Allocating and Recording the Estimated Accrual

The estimated accrual figure for obligated documents will be allocated to the general ledger accounts and funds in which the obligations were charged. The estimated accrual figure for direct charges will be allocated to the funds based on the percentage of charges of each fund to the total direct charges, ensuring compliance with applicable appropriation laws. Allocations are posted at the cost/asset level required by the Bureau/Departmental Office. Data analysis will continue to be evaluated throughout the current fiscal year to ensure that the estimated accrual amount is reasonable.

One of the selection criteria in this estimation process is capitalized property object class. When the computed accrual is allocated, that portion attributable to capitalized property must be recorded as an asset and not an expense. The appropriate general ledger entries should be made.