December 16, 2009

Memorandum

To: Members of the AAPC

From: Eileen W. Parlow, Assistant Director

Through: Wendy M. Payne, Executive Director


MEETING OBJECTIVES

To request that the AAPC consider a potential Technical Release that would describe a cost-effective framework for developing reasonable estimates of grant accruals. A Task Force representing federal agencies, federal auditors and independent public accountants developed the attached draft guidance.

BRIEFING MATERIAL

This memorandum provides a summary project history and a discussion of agency and auditor concerns. Attached to this memorandum are:

A. Working Draft: Guidance Developed by Grants Accounting Task Force and FASAB Staff (including list of Task Force and Working Group members)

B. Draft Project Plan Milestones

C. Minutes from Task Force Meeting held on December 8, 2009

D. Minutes from Task Force Meeting held on August 13, 2009

E. Historical Background:

1. Minutes from July 2007 AAPC Meeting
2. 2007 Survey responses from four Financial Statement Audit Network (FSAN) members:
   - Corporation for National and Community Service
   - Department of Energy
   - Department of Labor
   - National Aeronautics and Space Administration
BACKGROUND

Summary Project History

In May 2007, the Federal Transit Administration (FTA) submitted the FTA’s detailed grant accrual methodology asking for the AAPC’s review and comments. In addition, the FTC asked for guidance that would establish a methodology and validation technique for the federal accounting community. The AAPC agreed to discuss the issue at the July 2007 meeting.

At the July 2007 meeting, the DOJ provided information about their experience in developing grant accrual methodologies and auditor involvement. In addition, after the May 2007 meeting, Mr. Michael McFadden (Dept. of Labor) arranged to have a brief questionnaire sent to the FSAN members asking about their experiences with grant accruals, including estimates of FTEs in the audit work. The four responses received were shared with the AAPC members. In addition, the Department of Transportation withdrew the FTA’s request for guidance. The AAPC decided not to undertake a grants accounting project at that time.

In April 2009, three roundtables were held to hear the concerns of:

a) Preparers (Federal entities),
b) Auditors (Federal Offices of Inspector General (OIGs)) and
c) Independent Public Accountants

A Task Force with representatives from the above three groups met in August 2009 to discuss how to address the concerns expressed in the roundtables, all of which involved a need for cost-effective methods for developing grant accrual estimates.

FASAB staff developed initial draft guidance in September 2009, which a Task Force working group assisted to further develop. The attached draft guidance was reviewed by the entire Task Force (list of members is attached.)

Issues and Question for AAPC members

The Federal agencies and OIGs, as well as interested IPAs, have recommended that the FASAB provide guidance on cost-effective methods of performing reasonable estimates of grant accruals. Ideally, the guidance would address (a) developing estimates and (b) validating estimates with a goal of reporting reasonable estimates that are developed and validated in a cost-effective manner.

Accordingly, staff believes that it might be appropriate to further develop this guidance as a potential AAPC Technical Release.

However, if the AAPC members believe that the guidance should not be issued as an AAPC Technical Release, FASAB staff would develop the guidance as potential Staff Implementation Guidance.

**Question for AAPC members:**
Based upon the above, do you believe that the guidance should be developed as a potential AAPC Technical Release?

Attachments:
A. Working Draft: Guidance Developed by Grants Accounting Task Force and FASAB Staff (including list of Task Force and Working Group members)
B. Draft Project Plan Milestones
C. Minutes from Task Force Meeting held on December 8, 2009
D. Minutes from Task Force Meeting held on August 13, 2009
E. Historical Background:
Proposed Draft Guidance: Table of Contents

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Introduction

1. A series of roundtables in April 2009 indicated that guidance for estimating accruals for grant programs would be helpful for agencies. Specifically, agencies indicated a need for guidance that describes a cost-effective framework for developing reasonable estimates of accrued grant liabilities.

Scope

2. This Technical Release (TR) applies to grants that are paid by a federal entity to a non-federal entity. This TR does not apply to contracts or other purchases of goods or services. This TR does not establish new reporting requirements. This TR does not affect reporting in the Budget of the United States or special-purpose reports such as those required by law or regulation to be prepared in accordance with guidance other than generally accepted accounting principles.

Preparing Accrual Estimates for Grant Programs

3. Preparing reliable and timely accrual estimates for grant programs must be a joint effort between the budget, CFO and program offices at each agency. These offices should work together to ensure that the procedures and internal control recommendations\(^1\) outlined in this TR are implemented and operating as designed. However, some agencies may not be able to effectively implement all of these procedures, because they have not yet developed the necessary data stores and/or methods for preparing year-end accrual estimates. Therefore, until sufficient relevant historical information on all grant programs is available, the acceptable alternatives outlined in this TR should be utilized for developing year-end grant accrual estimates.

4. Each agency should document and maintain support for the data and assumptions used to develop the year-end grant accrual estimate. The documentation will facilitate the agency’s review of the assumptions, a key internal control, and will also facilitate auditor validation of the estimates. Documentation should be complete and stand on its own, i.e., a knowledgeable independent person could perform the same steps and replicate the same results. If the documentation were from a source that would normally be destroyed, then copies should be maintained in the file for the purpose of reconstructing the estimate.

5. For both existing grant programs and new or modified grant programs, management’s documentation of relevant program design factors may include

\(^1\) Internal control is an integral component of an organization’s management that provides reasonable assurance regarding the achievement of reliable financial reporting, effective and efficient operations, and compliance with applicable laws and regulations. Internal control consists of the control environment, risk assessment, control activities, information and communications and monitoring.
a. Program definition including legislation
b. Legislation or regulations changing the terms, maximum grant amount, total program size, or characteristics of the grantee population
c. Program eligibility requirements
d. Grant agreements detailing the terms and conditions of the grants

Preparing Accrual Estimates for Existing (Mature) Grant Programs

6. Agencies must accumulate sufficient relevant and reliable data on which to base accrual estimates. Each agency should prepare grant accrual estimates based upon the best available data at the time the estimates are made. Guidance on the types of supporting documentation that are acceptable for existing (mature) grant programs is found in paragraphs 5 and 7 of this document.

7. For existing programs, management should ensure that the following documentation is available for accrual estimates relating to existing grant programs:
   a. Procedures used for calculating the estimate
   b. Documentation for the review and approval process for the estimate
   c. Support for the calculation of the estimate, including the underlying assumptions used
   d. Historical supporting data used in the assumptions
   e. Documentation of relevant supporting actual cash and/or accrual experience (including the date and source of reports, whether grantees reported on a cash or accrual basis, and how recently the data were updated). The documentation may include:
      i. Historical data and trends, citing sources of information and relevant time frame
      ii. An analysis that identifies the most critical factors
      iii. Trend analysis developed from reports from the accounting or program management systems
      iv. Evidence of experience by other agencies with similar programs
      v. Evidence of emergencies or legislated changes, such as changes in program terms, program size, or characteristics of grant recipients
      vi. Evidence of other relevant factors that may be identified by grant program managers
   f. Explanation of the sampling process used, including if applicable treatment of grant programs with different payment patterns, and/or legislation.
g. Explanation of the calculation concept used, such as simple linear regression, statistical analysis, or other appropriate method

h. Procedures for error checking

i. Procedures for monitoring/validation subsequent to fiscal year-end

Preparing Accrual Estimates for New Grant Programs or Changes to Existing Grant Programs

8. In the absence of sufficient relevant and reliable historical data on which to base accrual estimates, agencies should prepare estimates based upon the best available data at the time the estimates are made. Paragraphs 5 and 11 of this document provide guidance on acceptable types of supporting documentation.

9. In certain limited instances, informed opinion may be used to support grant accrual estimates in the absence of sufficient relevant and reliable historical data. Informed opinion refers to the judgment of agency staff or others who make estimates based on their programmatic knowledge and/or experience without using a fully satisfactory information store and, in some cases, without using an econometric or other statistical model. Informed opinion may be used only as a last resort when relevant and reliable historical data and/or modeling capabilities are not available. This could occur when a new program has been established or when the Congress has changed an existing program in ways that cannot be represented by historical data. Informed opinion should therefore be used as an interim method only, and the agency should develop an action plan to establish an information store, appropriate models, and supporting documentation.

10. If an expert is used, the expert’s qualifications, such as professional or academic certification or length and kind of experience, must be assessed. The basis of the stated opinion must be articulated and documented in sufficient detail to allow review and validation by independent sources, including independent auditors. For example, a statistician may be best qualified to determine the appropriate model for year-end grant accrual estimates using limited or imperfect data.

11. Management should ensure that the following documentation is available for new programs or changes to existing programs that do not have historical supporting documentation. In the absence of relevant and reliable historical experience as the support for estimates, the agency should document the basis for accrual estimates. Typical support may include:

a. Relevant experience from other agencies, including documentation of why another agency’s experience is relevant, as well as similarities and differences (particularly possible biases) between the other agency’s experience and the new programs or changes to existing programs of the agency relying on the experience of the other agency
b. Extrapolation from subsets of prior program activity, e.g., while prior grants were not specifically targeted to a certain pool of grantees, it may be possible to identify prior activity with grantees with the same or similar characteristics to the targeted pool

c. Information from program managers regarding grantee activity and spending patterns

d. When expert opinion is used as an interim measure, the agency should document the expert’s qualifications, such as professional or academic certification or length of experience, as well as the basis for the stated opinion. In addition, the following documents should be maintained in support of the expert’s opinion:
   i. Reports and studies on relevant issues
   ii. Minutes from internal meetings and other relevant communications describing the basis for any assumptions or changes in assumptions.

Display

12. When grant accrual estimates are prepared on the level of individual grantee, advances and accrued liabilities associated with the same grantee should be reported as a net figure on the balance sheet. In such instances, no disclosure of disaggregated amounts would be required.

13. When grant accrual estimates are prepared on an aggregate level, agencies may display a net amount on the balance sheet and report estimated disaggregated advances and liabilities in a note. (An illustrative example is displayed in Appendix B.)

Internal Controls: Developing Grant Accrual Estimates

14. Agencies should document the procedures and flow of information used in developing grant accrual estimates at a high level, e.g. flow chart with supporting narrative. These documents should be used to establish consistent procedures for developing grant accrual estimates across grant programs with similar characteristics. These documents should also include a discussion of who is responsible for each step of the estimate as well as the review and approval process followed. Documented procedures are necessary to communicate relevant information on the grant accrual estimation to employees as well as other interested parties, such as auditors. As an agency experiences employee turnover, these documented procedures will provide vital information for new employees on how to complete reliable, well supported grant accrual estimates.

15. Agencies should document the model(s) used, the rationale for selecting the specific methodologies, and, for programs with sufficient historical data, the
degree of calibration within the projected spending model(s). Agencies should also document the sources of information, the logic flow, and the mechanics of the model(s), including the formulas and other mathematical functions. In addition, agencies should document the controls over the model(s) used by the agency in preparing worksheets.

16. Agencies should maintain detailed subsidiary accounting records by grant program. Agencies should have an audit trail from individual transactions to the subsidiary ledgers to the general ledger.

17. Management should assess the impact of changes in law or regulations on the reliability of estimates and should ensure that the grant accrual estimate model reflects these changes.

18. Management should assess the impact of subsequent events on their grant accrual estimates. Some subsequent events may require adjustments to the financial statements while others may require disclosure in the notes to the financial statements.

19. Procedures in place should ensure that grant accrual estimates are based on historical transactions in previous years to the extent that relevant and reliable historical data exists.

20. The grant accrual estimation process, including underlying assumptions, should be reviewed and approved at the appropriate level. The agency should perform a trend analysis of grant accrual estimates from year to year. When unusual fluctuations are identified, they should be investigated.

**Monitoring Internal Controls**

21. Management should monitor controls to determine whether they are operating as intended and that they are modified as appropriate for changes in conditions. Monitoring is a process that assesses the quality of internal controls performance over time. The Office of Management and Budget (OMB) Circular A-123, *Management’s Responsibility for Internal Control*, is issued under the authority of the Federal Managers’ Financial Integrity Act (FMFIA) of 1982 and provides guidance to federal managers on improving the accountability, efficiency and effectiveness of federal programs and operations by establishing, assessing, correcting, and reporting on management controls. Circular A-123 provides that:

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2 Calibration is the degree of precision within the model, i.e., the model’s ability to accurately predict the trends of expenses incurred for a given grant program. The degree of calibration within the model can be documented by charts or graphs showing projected expenses incurred versus the actual expenses incurred by reporting period. This document would analyze the variance between projected and actual expenses incurred by grantees.

3 At this time, subsequent events are addressed in other accounting literature and in auditing standards but not in federal accounting standards. However, the Board has proposed requirements for subsequent events. See FASAB Exposure Draft: *Subsequent Events: Codification of Accounting and Financial Reporting Standards Contained in the AICPA Statements on Auditing Standards*, October 20, 2009.
Instead of considering internal control as an isolated management tool, agencies should integrate their efforts to meet the requirements of the FMFIA with other efforts to improve effectiveness and accountability. Thus, internal control should be an integral part of the entire cycle of planning, budgeting, management, accounting, and auditing. It should support the effectiveness and the integrity of every step of the process and provide continual feedback to management.

Federal managers must carefully consider the appropriate balance between controls and risk in their programs and operations. Too many controls can result in inefficient and ineffective government; agency managers must ensure an appropriate balance between the strength of controls and the relative risk associated with particular programs and operations. The benefits of controls should outweigh the cost. Agencies should consider both qualitative and quantitative factors when analyzing costs against benefits.4

**Validation of Grant Accrual Estimates**

22. As part of agencies’ internal control procedures to ensure that grant accrual estimates are reasonable, agencies should validate grant accrual estimates by comparing the estimates with subsequent grantee reporting.

23. When validating the reasonableness of accrual estimates, an agency does not need to obtain data5 from 100% of grantees in order to validate the reasonableness of grant accrual estimates. For example, agencies may validate estimates based upon:
   a. grantee data that represents a reasonable majority of the total grant portfolio, or
   b. data from a statistically valid sampling of the total grantee portfolio.

24. When developing grant accrual estimates, agencies should consider data that is available at the time. The validation process includes an understanding that estimates are inherently uncertain, and that management must use judgment in determining:
   a. whether differences between estimated and actual expense are reasonable, and
   b. if different estimation methods could result in more accurate estimates in the future.

25. AICPA [proposed] audit guidance states that:
   a. A difference between the outcome of an accounting estimate and the amount originally recognized in the financial statements does not

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5 Data refers to information about actual grantee expenses. Sources of data may include but are not limited to grantee reports to agencies and audited accruals from Single Audit Act audits.
necessarily represent a misstatement of the financial statements; rather, it could be an outcome of estimation uncertainty\(^6\) and that

b. Differences between estimates and actual should be taken into consideration in developing the subsequent period's estimate.\(^7\)

**Training and Monitoring of Grantees**

26. Since preparation of accrual estimates is dependent upon relevant and reliable data, accurate and timely reporting by grant recipients serves as the basis for historical data used in preparing future estimates and provides reliable actual data to which accrual estimates can be compared. Agencies should ensure that grant recipients receive training on completing required financial reports. Training may be delivered via agency sponsored conferences, workshops and/or seminars, customer service centers and help desks, or computer based sources such as webcasts or other training options available through the agency’s website. Adequate training of grantees results in greater accuracy and timely submission of financial reports.

27. Reports submitted by grantees should be reviewed to ensure their reasonableness. Agencies should have policies and procedures in place to review and verify the grantee expenditures reported.

28. When agencies engage in on-site financial monitoring of grantees, protocols should include verifying grant expenditures reported with actual expenditures posted in the grantee’s accounting system. Techniques for monitoring of grantee reporting of expenditures may also include stratified sampling.

29. Timely follow up of incorrect reporting should be performed to ensure a higher degree of compliance with reporting requirements. For example, inaccurate grant expenditures reported could be conveyed to grantees by an official letter requesting a corrective action plan. During on-site financial reviews, technical assistance could be provided when grant expenditures reported are inaccurate.

**Materiality Considerations and Risk Assessment**

30. SFFAS 3, paragraph 14, states that “the accounting and reporting provisions of…standards should be applied to all items that would influence or change the users’ judgment of the entity’s efficiency and effectiveness and its compliance with laws and regulations in a material manner.”\(^8\) In particular,


\(^{7}\) Note that the AICPA audit guidance notes that the review of the outcome of accounting estimates “is not intended to call into question the judgments made in the prior periods that were based on information available at the time.” (Ibid., paragraph 9.)

\(^{8}\) SFFAS 3, paragraph 14. See Attachment 1 for the full discussion of materiality from SFFAS 3.
management should consider the materiality of the grant program relative to
to the agency’s statement of net cost.

31. The following list includes some of the factors that management should
consider in determining which grant programs may have a higher risk of
material misstatement that might cause financial statement users to make
incorrect assessments regarding the efficiency and effectiveness of the
program:

a. the degree of variance between past estimates and the program’s actual
operating cost (if applicable),
b. significant findings reporting in past program audits (if applicable),
c. the age of the program (other factors being equal, mature programs may
have less risk than newer programs),
d. Congressional and other public policy interest in a given program.

32. For grant programs that are immaterial to the statement of net cost and/or
that have a lower risk of misstatement, management might consider
validating estimates at less frequent time intervals.

33. Management should use judgment in determining the appropriate investment
of time and effort that should be devoted to the process of estimating
accruals for grant programs or other activities.

34. Statements of Federal Financial Accounting Concepts (SFFACs) represent
guidance for the Board in developing accounting standards. SFFAC 1 states
that: “the accrual basis of accounting generally provides a better matching of
costs to the production of goods and services, but its use and application for
any given purpose must be carefully evaluated.”

35. SFFAC 1 also discusses balancing costs and benefits in recommending
standards. For example, it states that

…the process of articulating financial reporting objectives and then
recommending accounting standards is not a simple progression from
canvassing users of federal financial information to recommending standards
…because articulating objectives and recommending accounting standards
necessarily involve judgments about the costs and benefits of producing more
information or of reporting it differently.

…Finally …accounting and financial reporting cannot satisfy every need for
information and accountability. For many purposes, other information
sources and other techniques to maintain and demonstrate accountability are
either essential or more cost-effective. This constraint pervades any
discussion of the objectives of federal financial reporting.

9 SFFAC 1, par. 197.
10 SFFAC 1, par. 151.
11 SFFAC 1, par. 155.
36. This example decision tree diagram illustrates processes that agencies might use in the grant accrual process. This example is illustrative only and is not authoritative guidance.

Figure 1: Illustrative Example of Grant Accrual Process
37. This example decision tree diagram illustrates processes that agencies might use in verifying grant accrual estimates. This example is illustrative only and is not authoritative guidance.

Figure 2: Illustrative Example of Validation/Verification Process

Obtain reports from a sufficient proportion of grantees that correlate to the reporting period that was estimated. (See paragraph 23 of this TR.)

If reports represent less than 100% of grantees, perform an analysis and project available actual data to the estimate.

Is difference material to financial statements?

Yes

Was difference caused by misuse of information available at the time? *

Yes

Approve estimate and document verification.

No

- Restate prior period financial statements.
- Update data used to calculate accrual estimate for future periods.
- Consider updating process for estimating accruals.

- Incorporate adjustment into current period estimate
- Update data used to calculate accrual estimate for future periods.
- Consider updating process for estimating accrual.

No

Appendix A: Basis for Conclusions

Project History

A1. A series of roundtables in April 2009 indicated that guidance for estimating accruals for grant programs would be helpful for agencies. Specifically, agencies indicated a need for guidance that describes a cost-effective framework for developing reasonable estimates of accrued grant liabilities.

A2. A Task Force consisting of representatives from federal agencies and independent accounting and consulting firms assisted FASAB staff in identifying areas where guidance would be helpful. A list of Task Force members appears at Appendix D.

A3. Proposed draft guidance was submitted to the FASAB’s Accounting and Auditing Policy Committee (AAPC) for consideration at the January 2010 AAPC meeting.
Appendix B: Illustrative Example of Note on Netting Grant Advances and Accrued Liabilities

Paragraph 13 of this TR states that: when grant accrual estimates are prepared on an aggregate level, agencies may display a net amount on the balance sheet and report estimated disaggregated advances and liabilities in a note. Below is an illustrative example of such a note.

Note XX: Net Grant Liability

The [reporting entity] awards grants to various grantees and provides advance payments to meet grantees' cash needs to carry out the [reporting entity's] programs.

For grants subject to grant expense accrual, grantees draw funds (recorded as advances to grantees) based on their estimated cash needs. As grantees report their actual disbursements quarterly, the amounts are recorded as expenses, and their advance balances are reduced. In some instances, grantees incur expenditures before drawing down funds that, when claimed, would reduce the advances to grantees account to a negative balance. An accrued grant liability occurs when the accrued grant expenses exceed the outstanding advances to grantees.

At year-end a grant accrual estimate is developed based upon actual payments made through the fourth quarter and an unreported grant expenditure estimate for the fourth quarter based on historical spending patterns of the grantees. The year-end accrual estimate equals the estimate of fourth quarter disbursements plus an average of xx weeks of annual expenditures for expenses incurred prior to the cash being drawn down.

<table>
<thead>
<tr>
<th>Accrued Grant Liability (In Millions)</th>
<th>2009</th>
<th>2008</th>
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<tr>
<td>Grant Advances Outstanding (before year-end grant accrual)</td>
<td>$ XX,XXX</td>
<td>$ XX,XXX</td>
</tr>
<tr>
<td>Less: Estimated Accrual for Amounts Due to Grantees</td>
<td>(XX,XXX)</td>
<td>(XX,XXX)</td>
</tr>
<tr>
<td>Net Grant Advances (Liability)</td>
<td>$ (X,XXX)</td>
<td>$ (X,XXX)</td>
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Appendix C: Relevant Citations of Existing Guidance


1. An asset is a resource that embodies economic benefits or services that the federal government controls.  
2. A liability is a present obligation of the federal government to provide assets or services to another entity at a determinable date, when a specified event occurs, or on demand.

Statement of Federal Financial Accounting Standards (SFFAS) 1, Accounting for Selected Assets and Liabilities, defines advances as cash outlays made by a federal entity to its employees, contractors, grantees, or other to cover a part or all of the recipients’ anticipated expenses or as advance payments for the cost of goods and services the entity acquires. Examples include travel advances disbursed to employees prior to business trips, and cash or other assets disbursed under a contract, grant, or cooperative agreement before services or goods are provided by the contractor or grantee.

SFFAS 5, Accounting for Liabilities of the Federal Government, states that:

[24.] A nonexchange transaction arises when one party to a transaction receives value without directly giving or promising value in return. There is a one-way flow of resources or promises. For federal nonexchange transactions, a liability should be recognized for any unpaid amounts due as of the reporting date. This includes amounts due from the federal entity to pay for benefits, goods, or services provided under the terms of the program, as of the federal entity’s reporting date, whether or not such amounts have been reported to the federal entity (for example, estimated Medicaid payments due to health providers for service that has been rendered and that will be financed by the federal entity but have not yet been reported to the federal entity).

[25] Many grant and certain entitlement programs are nonexchange transactions. When the federal government creates an entitlement program or gives a grant to state or local governments, the provision of the payments is determined by federal law rather than through an exchange transaction.

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12 SFFAC 5, par. 18.
13 SFFAC 5, par. 39.
14 SFFAS 1, par. 37.
15 SFFAS 5, Footnote [12] Goods or services may be provided under the terms of the program in the form of, for example, contractors providing a service for the government on the behalf of the disaster relief beneficiaries.
SFFAS 5 requires that for grant programs, the liability that should be reported includes the amount of allowable expense that the grantees have incurred as of the end of the period, but have not collected from the agency. Complying with SFFAS 5 requires that the agency estimate the amounts not reported by the grantee but due to the grantee as of the reporting date. When the grantee has submitted reports providing the grantee’s actual costs, the federal agency will be able to assess the grantee reports for accuracy and/or analyze the agency’s estimate for accuracy.

SFFAC 3 on MATERIALITY

[7.] The Board intends that the standards' application be limited to items that are material. "Materiality" has not been strictly defined in the accounting community; rather, it has been a matter of judgment on the part of preparers of financial statements and the auditors who attest to them. The Board proposes relying on the Financial Accounting Standards Board's (FASB) concept as modified by certain concepts expressed in governmental auditing standards. Presented below is the Board's position on the issue of materiality at this time.

[8.] The accounting and reporting provisions of the Board's accounting standards need not be applied to immaterial items. The determination of whether an item is immaterial requires the exercise of considerable judgment, based on consideration of specific facts and circumstances.

[9.] FASB's Statement of Accounting Concepts No. 2, "Qualitative Characteristics of Accounting Information," discusses the concept of materiality. According to this statement, the determination of whether an item is material depends on the degree to which omitting or misstating information about this item makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or the misstatement. This concept includes both qualitative and quantitative considerations. An item that is not considered material from a quantitative standpoint may be considered qualitatively material if it would influence or change the judgment of the financial statement user.

[10.] The Board believes that FASB's definition of materiality is generally appropriate for use in applying the accounting and reporting provisions of the Board's accounting standards. In the federal government environment, however, the definition is extended to apply to all financial information included in the annual financial report and, therefore, is not limited to the principal schedules and related notes.

[11.] In applying the concept of materiality, the needs of the users of the annual financial report should also be considered. In the federal government environment, such needs generally differ from those of users of commercial entity financial statements. For example, federal government financial statement user needs extend to having the ability to assess the efficiency and the effectiveness of the entity's programs. Further, compliance with budget and other finance-related laws, rules, and regulations is also a significant consideration of such users.

[12.] This is expressed well in the Government Auditing Standards (the "Yellow Book"):
"In government audits the materiality level and/or threshold of acceptable risk may be lower than in similar-type audits in the private-sector because of the public accountability of the entity, the various legal and regulatory requirements, and the visibility and sensitivity of government programs, activities, and functions." (Ch. 3, par. 33.)

[13.] While this standard applies to an auditor's evaluation of materiality rather than a preparer's, it does provide insight into the factors affecting materiality in the federal government.

[14.] Therefore, the accounting and reporting provisions of the Board's recommended standards should be applied to all items that would influence or change the users' judgments of the entity's efficiency and the effectiveness and its compliance with laws and regulations in a material manner.

[15.] In order to emphasize that materiality should be considered in applying all accounting standards, the Board has decided to place a notice at the end of each recommended accounting standard. The notice will read as follows:

| The provisions of this statement need not be applied to immaterial items |
## Appendix D: Grants Accounting Task Force Members

### Grants Accounting Task Force Members

#### Working Group:

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<th>Organization</th>
<th>Name</th>
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<tbody>
<tr>
<td>Department of Health and Human Services</td>
<td>Patricia Irving</td>
</tr>
<tr>
<td>DJ Business Solutions</td>
<td>Denise Joseph</td>
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<tr>
<td>Department of Transportation</td>
<td>Katherine Lambert</td>
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<td>Grant Thornton LLP</td>
<td>Shal Malhotra</td>
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<td>Kforce Government Solutions</td>
<td>Jim McKay</td>
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<td>KPMG LLP</td>
<td>Derek Thomas</td>
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<tr>
<td>Clifton Gunderson LLP</td>
<td>Denise Wu</td>
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</table>

#### Task Force: Federal Agencies

<table>
<thead>
<tr>
<th>Agency</th>
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<tbody>
<tr>
<td>Department of Agriculture</td>
<td>Whitney, Tyson</td>
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<td>U.S. Agency for International Development</td>
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<td>U.S. Agency for International Development Lowe, Roberta</td>
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<tr>
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<td>Alston, Gordon</td>
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<td>Corporation for National and Community Service</td>
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<td>Corporation for National and Community Service OIG</td>
<td>Axenfeld, Stuart</td>
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<td>Defense Finance and Accounting Service</td>
<td>Hill, Travis</td>
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<td>Department of Education</td>
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<td>Environmental Protection Agency</td>
<td>Benett, Richard</td>
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<td>Curtis, Paul</td>
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<td>Vass, Catherine</td>
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<td>Environmental Protection Agency</td>
<td>Visnik, Melvin</td>
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<td>Executive Office of the President, Office of Administration</td>
<td>Buhler, Mary</td>
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<tr>
<td>Executive Office of the President, Office of Administration</td>
<td>Smith, Giovonni Hargrave</td>
</tr>
<tr>
<td>General Services Administration</td>
<td>Andre, John</td>
</tr>
</tbody>
</table>

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## Attachment A: Appendix D Task Force Members

| Government Accountability Office | Anderson, Phyllis  
|                                | Nowicki, Jacqueline |
| Department of Health and Human Services | Chaves, Helio  
|                                | Dawson, Molly  
|                                | Irving, Patricia  
|                                | Lee, Katherine |
| Department of Health and Human Services OIG | Cox, Cathy  
|                                | Moadel, Mark |
| Department of Housing and Urban Development OIG | Collymore, A.  
|                                | Heist, J.  
|                                | McEnanly, T.  
|                                | McGinnis, R.  
|                                | Moore, Andrea  
|                                | Stamps, Narcell |
| Department of Justice | Paull, Marcia  
|                                | Ramos, Frank  
| Department of Justice OIG | Lassiter, Jermaine  
| Department of Labor OIG | Donovan, Joseph  
| National Aeronautics and Space Administration | Calhoun, Juanakee  
|                                | Jenson, Mark  
|                                | Robertson, Michelle |
| National Science Foundation | Lynskey, John  
|                                | Ruffin, Shirl |
| Office of Management and Budget | Kearney, Regina  
| Small Business Administration | Brindle, Jeff  
|                                | Ritt, Debra |
| Department of Transportation | Angel, Robert  
|                                | Lambert, Katherine  
|                                | Lampkin, Teresa  
|                                | Leiphart, Kristine  
|                                | Nwosu, Godwin  
|                                | Sheridan, Margo |
| Department of Transportation OIG | Banks, George  
|                                | Hedges, Earl  
|                                | Leng, Rebecca |
| Department of the Treasury | Bell, Scott |
### Task Force: Independent Public Accountants and Consulting Firms

<table>
<thead>
<tr>
<th>Firm</th>
<th>Members</th>
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<tbody>
<tr>
<td>Clifton Gunderson LLP</td>
<td>Wu, Denise</td>
</tr>
<tr>
<td>DeLoitte &amp; Touche LLP</td>
<td>Cooper, Renee</td>
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<td>Duquette, Dennis</td>
</tr>
<tr>
<td>DJ Business Solutions</td>
<td>Joseph, Denise</td>
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<td>Grant Thornton LLP</td>
<td>Cox, John</td>
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<td></td>
<td>Malhotra, Shal</td>
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<td></td>
<td>Williams, Clifton</td>
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<tr>
<td>Kearney &amp; Company</td>
<td>Zavada, Dave</td>
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<tr>
<td>Kforce Government Solutions</td>
<td>McKay, Jim</td>
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<td>KPMG LLP</td>
<td>Kovlak, Daniel</td>
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<td>Longo, Ron</td>
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<td>Supernaw, Catherine</td>
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<td>Thomas, Derek</td>
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<td>PricewaterhouseCoopers</td>
<td>Fennell, Walt</td>
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<td></td>
<td>Kull, Joseph</td>
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<td>McNamee, Pat</td>
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Attachment B: Draft Project Plan Milestones

## Draft Project Plan Milestones

<table>
<thead>
<tr>
<th>Date Range</th>
<th>Event Description</th>
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<tbody>
<tr>
<td>April 28-30, 2009</td>
<td>Roundtable Meetings</td>
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<tr>
<td>August 13, 2009</td>
<td>Task Force Kickoff Meeting</td>
</tr>
<tr>
<td>October 2, 2009</td>
<td>Staff draft to Working Group</td>
</tr>
<tr>
<td>October 5 – October 20, 2009</td>
<td>Review/Comments from Working Group</td>
</tr>
<tr>
<td>October 28, 2009</td>
<td>Revised guidance and summary of comments to Working Group responders (comments due November 6)</td>
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<tr>
<td>November 6- November 17, 2009</td>
<td>Staff and Working Group collaborate on revised draft guidance/AAPC proposal</td>
</tr>
<tr>
<td>November 18, 2009</td>
<td>FYI copy of current draft to full Task Force (Comments due December 3)</td>
</tr>
<tr>
<td>December 8, 2009</td>
<td>Task Force Meeting/Teleconference to finalize proposal for AAPC</td>
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<tr>
<td>December 9 – December 15, 2009</td>
<td>Staff and Task Force collaborate (if needed) to finalize draft guidance/AAPC proposal</td>
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<tr>
<td>December 16, 2009</td>
<td>Material to AAPC with request to be on AAPC agenda for January 2010 meeting</td>
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<tr>
<td>January 21, 2010</td>
<td>AAPC to consider whether to accept project and proposal</td>
</tr>
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</table>

### A. Continuation of timeline if project is accepted by the AAPC

<table>
<thead>
<tr>
<th>Date Range</th>
<th>Event Description</th>
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<tbody>
<tr>
<td>January to March, 2010</td>
<td>Work with AAPC members to finalize ED</td>
</tr>
<tr>
<td>March 18, 2010</td>
<td>AAPC issues ED for TR</td>
</tr>
<tr>
<td>April 2010</td>
<td>Comments due for ED</td>
</tr>
<tr>
<td>May 20, 2010</td>
<td>AAPC finalizes proposed TR</td>
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<tr>
<td>June 30, 2010</td>
<td>Proposed TR to Board for review</td>
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<tr>
<td>July 2010</td>
<td>AAPC issues TR</td>
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### B. Continuation of timeline if project is not accepted by the AAPC

<table>
<thead>
<tr>
<th>Date Range</th>
<th>Event Description</th>
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<tbody>
<tr>
<td>January- March 2010</td>
<td>Staff and working group develop draft SIG</td>
</tr>
<tr>
<td>April 2010</td>
<td>SIG for public comment</td>
</tr>
<tr>
<td>May 2010</td>
<td>SIG to Board for review</td>
</tr>
<tr>
<td>June 2010</td>
<td>(If approved) SIG issued</td>
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Attachment C: Minutes from Task Force Meeting on December 8, 2009

Note: The December 8, 2009 meeting was brief. Several attendees arrived after the initial meeting had been adjourned. Accordingly, attendees are listed under Part 1 and Part 2.

Attendees, Part 1 of Meeting

<table>
<thead>
<tr>
<th>Organization</th>
<th>Represented by:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Department of Commerce</td>
<td>Susan Crippen</td>
</tr>
<tr>
<td>Grant Thornton</td>
<td>John Cox</td>
</tr>
<tr>
<td>National Aeronautics and Space Administration</td>
<td>Yolanda Keiller</td>
</tr>
<tr>
<td>National Science Foundation</td>
<td>John Lynsky</td>
</tr>
<tr>
<td></td>
<td>Gene Kim</td>
</tr>
<tr>
<td></td>
<td>Cynthia Paolillo</td>
</tr>
<tr>
<td>FASAB staff</td>
<td>Eileen Parlow</td>
</tr>
<tr>
<td></td>
<td>Wendy Payne</td>
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Attendees, Part 2 of Meeting

<table>
<thead>
<tr>
<th>Organization</th>
<th>Represented by:</th>
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<tbody>
<tr>
<td>Department of Justice</td>
<td>Frank Ramos</td>
</tr>
<tr>
<td></td>
<td>Joanne Suttington</td>
</tr>
<tr>
<td>Department of Justice Office of Inspector General</td>
<td>Jermaine Lassiter</td>
</tr>
<tr>
<td>DJ Business Solutions</td>
<td>Denise Joseph</td>
</tr>
<tr>
<td>FASAB staff</td>
<td>Eileen Parlow</td>
</tr>
</tbody>
</table>

Minutes: Part 1 of Meeting

FASAB staff Ms. Parlow called attention to the Project Milestones and noted that the proposed TR will be the agenda at the January 21, 2010 AAPC meeting, at which time the AAPC will decide whether to accept this project. She said that there will be future opportunities to comment on the draft guidance, regardless of whether it is developed as a proposed FASAB Accounting and Auditing Policy Committee (AAPC) Technical Release (TR) or as proposed FASAB Staff Implementation Guidance.

One participant said that it was important that netting of grant advances and accrued liabilities should not be mandatory, but said that the proposed wording (“may”) is adequately clear.

Ms. Parlow asked if participants wished to volunteer to assist the AAPC if the AAPC accepts the project. The representatives from the Department of Commerce, the National Science Foundation and Grant Thornton indicated in the affirmative. Those representatives also voted to approve the draft guidance, including the draft guidance on netting. The National Aeronautics and Space Administration was representative said that she was new to the project and needed to abstain from voting.

Minutes: Part 2 of Meeting

FASAB staff Ms. Parlow gave a brief recap of Part 1 of the meeting to the participants who arrived after the Part 1 of the meeting had adjourned. One participant noted a grammatical clarification to the illustrative note: that the last line of the table should say “Net Grant Advances (Liability)” instead of “Net Grant Liability.”

The participants at Part 2 of the meeting indicated approval of the draft guidance, including the draft guidance on netting, and also indicated that they would be available to assist the AAPC with this project in the future.
Grants Accounting Task Force Meeting
Detailed Minutes: August 13, 2009

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Methods of Calculating Estimates ........................................................................... 2
Focus on Net Cost (versus Balance Sheet)............................................................. 3
Types of Grants: Mandatory Grants and Other Formula Grants ........................... 4
Focus on Net Cost (versus Balance Sheet) - Continued........................................ 5
Why is this project being initiated? ......................................................................... 5
“Reasonable Estimate”............................................................................................. 6
Next Steps.................................................................................................................. 8
   Plans for the Working Group.................................................................................... 8
   Volunteers for Working Group.................................................................................. 9
FASAB Discussion Points for working group meeting........................................ 10
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Participants 8-13-2009 Task Force Meeting:

<table>
<thead>
<tr>
<th>Name</th>
<th>Organization</th>
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<tbody>
<tr>
<td>Allen, Charles*</td>
<td>Dept. of Education</td>
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<tr>
<td>Anderson, Phyllis</td>
<td>GAO</td>
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<tr>
<td>Ángel, Robert</td>
<td>DOT/FAA</td>
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<td>Banks, George</td>
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<td>Cox, Cathy</td>
<td>HHS OIG</td>
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<tr>
<td>Ganao, Felicity*</td>
<td>Dept. of Education</td>
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<tr>
<td>Hug, Carrie</td>
<td>Treasury Dept.</td>
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<td>Huritz, Ron</td>
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<td>Kearny, Regina</td>
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<td>Lambert, Katherine</td>
<td>DOT/FTA</td>
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<td>DOJ OIG</td>
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<td>Lynskey, John</td>
<td>NSF (via telephone)</td>
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<td>Kforce Gov’t Solutions</td>
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<td>Nwosu, Godwin</td>
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Introduction and Working Goals

Wendy Payne thanked the participants and noted that FASAB’s accomplishments in this project would be largely dependent upon the members of the Task Force. She said that participants could use the Task Force as an opportunity to resolve long-standing problems in grants accounting and introduced the project manager, Eileen Parlow.

Eileen Parlow asked if the group had any comments on the draft working goals: to identify major categories of grants and to identify best practices that might help improve quality and/or make the process less costly and to identify audit issues. Lastly, the group could propose guidance – not necessarily FASAB guidance- to improve grants accounting. She said that identifying categories of grants might be helpful because it does not seem likely that there will be a “one-size-fits-all” solution for issues that are identified. She said that FASAB staff is not aware of any identified problems with FASAB guidance but that any problems identified could also be addressed.

Methods of Calculating Estimates

An IPA representative said that at the agency where she is most experienced, the varieties of grants were huge. She said that at that agency they took a sample of a diverse set of grants and sent a questionnaire to the programs heads [for the selected grants] asking about drawdown patterns, grantee spending patterns, materiality of the potential grant accrual to the financial statements, etc.
She said that she had drafted a plan that might include sending out questionnaires to the community, and possibly engage in interviews with the community, and then put them into a decision matrix. She said that if fit a certain criteria— for example, if it is immaterial, then you do a footnote but you don’t do any estimation. She said that this group should come up with a proposal for what to do when the potential accrual could be material to the financial statements.

For example, for a new program, the estimate could be based on a weighted average distribution relative to the draw-down period. For longer programs, there can be a trend analysis which would be audited. She said that unless there are material improper payments, she has not seen much in terms of money being recovered. Because of this, she is wondering why not develop an across-the-board estimate using a method that everyone could agree on.

A federal preparer said that her agency has over 10,000 grantees and that the estimate is done in the system, grant by grant. Then every quarter they look at the 269s and see how their estimate compared with the data in the 269s.

Focus on Net Cost (versus Balance Sheet)

Another federal preparer said that one audit issue is that many auditors are balance-sheet focused rather than focused on the Statement of Net Cost (SNC). She said that she would like to see guidance that helps to clarify what is the best available information. This may be difficult because of the differences in system capabilities that differ widely among agencies.

A federal preparer said that in the private sector there is industry-specific audit guidance and that such guidance would be helpful relative to the federal government. He said that in his opinion grants should be expensed up-front. He said that generating the accrual gives an illusion of false precision.

Another federal preparer said that his suggestion would require a change in the standards.

Ms. Payne said that she spoke with a Board member who has criticized the cost of the process but that even that Board member would not support rescinding the requirement to accrue a payable for grants. Accordingly, she wants the group to understand that the goal of this project is not to recommend rescinding the requirement. She said that she had been somewhat more open to that possibility before the roundtables, but that during the roundtables it became apparent that the performance measure that Congress and the public are interested in is the cost of programs, for which the accrual is necessary information.

A federal preparer said that for many programs, the cost is similar from year to year.
Ms. Payne noted that this year is an example of how costs can be very different from year to year. The federal preparer said that anomalies like the Recovery Act can be handled differently, but for most programs, except for the first and last years, the cost is similar from year to year.

**Types of Grants: Mandatory Grants and Other Formula Grants**

Ms. Parlow asked if there are any categories of grants where it does not matter whether the grantee has spent the money or not – where the recipient gets the funds and does not have to report back on spending it.

An IPA representative said that there are. She said that mandatory grants. HHS has some of those - Medicare, Medicaid, Federal Highway all have formulas that are distributed to the states.

The IPA representative said that getting back to the audit issues, she would be concerned about changing standards from accrual basis to cash basis.

Ms. Parlow asked if all formula grants were mandatory. A federal preparer replied that some formula grants are not mandatory, although the very largest ones – such as Medicare and Medicaid - are mandatory.

Ms. Parlow said that a common process for accruals is to look at disbursements that were made during a period of time after the close of the reporting period. She asked if that process does not work well for grants.

A federal preparer said that there are a huge number of grantees and that the cycle is sometimes slow compared with the deadlines for the audited financial statements.

A federal preparer said that for the Recovery Act, the required reporting by grantees is cash-basis (in other words, how much the grantee has paid out, not accrued in expenses). So there is a question how to deal with that bias, and also the grantees have 10 days to report which is difficult because of the short turnaround time for agency financial statements. However, because the process is automated, it does not take a large amount of time.

Another federal preparer said that amounts obligated end up being spent, and that even amounts recovered are generally re-obligated and spent - for example, in no-year programs.

An IPA representative said that in some instances, material amounts recovered are returned to the Treasury.

Addressing the degree of precision needed, the IPA representative said that in her opinion the estimate should be “reasonable.” However, some auditors may be looking for a degree of precision that may go beyond that. She said that the audit guidance needs to clarify what degree of precision is needed. She said that auditors need to look
at the big picture. She said that many agencies have developed excellent methods for estimating the accrual.

Focus on Net Cost (versus Balance Sheet) - Continued

The IPA representative said that at the beginning of credit reform, there was a great deal of difficulty in getting the estimate on the books and passing audit, but now agencies follow a consistent methodology and calculate the subsidy using the OMB model and now the process of estimating the credit subsidy estimate is going smoothly. She said that it would be very helpful if there was an approved methodology that agencies could follow.

Another IPA representative said that the focus of credit reform was net cost, but that in contrast - reporting requirements focused on the balance sheet (definition of asset and liability) forces agencies to gross up receivables and payables for grants rather than report the net figure. She said that it would make a lot more sense to focus on net cost.

The IPA representative said that many agencies only have either advances or reimbursements but not both. However, she agreed that the focus should be on net cost rather than the balance sheet. She also said that The Cash Management Improvement Act generally prevents grantees from having huge amounts of money on hand without the need to spend the money because they only have three days to spend the money.

Why is this project being initiated?

A federal auditor said that doesn’t the fact that most agencies have been getting clean opinions indicate that there are no major issues with how this is being done? He said that he is not aware of any hubbub about the grant accrual process. He asked Ms. Payne the reason why FASAB is initiating this project.

Ms. Payne that the CFO survey that is done by AGA is one reason. She said that for about the last five years there have been complaints that accrual accounting costs too much for what we are getting out of it. She said that she does not necessarily endorse that view. She said that complaints particularly focused in the grant accrual. She said that also at the CFO Council meetings participants have called for greater efficiencies. She said that perhaps the accounting standards are driving inefficiencies such as grossing up receivables and payables. She said that perhaps there are more efficient ways to comply with a model that’s been sanctioned by a GAAP standard-setting body. Would that make it more efficient in relation to the perceived benefit? She mentioned that the roundtables indicated that there are perceived benefits. She said that she initiated the roundtables when one of the Board members consistently spoke publicly at large gatherings of accountants about “what a waste” of resources. She said that when controversy is being generated that we need to do examine the issue.
Ms. Payne said that two of participants had previously briefed the FASAB’s Accounting and Auditing Policy Committee. She said that one agency had previously come forward and then pulled back on a request for guidance on grant accruals.

An IPA representative said that agencies have said that some auditors have been asking them to reconcile their estimate with an HHS system estimate versus what the agencies themselves have calculated.

“Reasonable Estimate”

One federal preparer said that his agency had been involved in the request for guidance. He said that his agency had recently changed auditors and that the previous auditor had been satisfied with the grant accrual process but that the new auditor expected them to contact each grantee, which was simply not possible with the number of grantees and their current level of staffing. He said that it would be extremely helpful if auditors had a consistent way of looking at these grant accruals.

A federal auditor said that he thinks that we should drop the word “consistent” from this entire discussion because it is not feasible given the variety of different kinds of grants in the federal government. He pointed to AU 342 (on page 15 of the Task Force briefing materials) which says that the estimate should be “reasonable” and that should be the focus. He said it is important for this group to set some parameters for what is “reasonable.” The other federal preparer agreed.

An IPA representative agreed with the “reasonable” concept rather than a “consistent” methodology. He said that in the first few years, the methodology might change as the agency develops its understanding of the trends etc. within various grant programs, especially new programs. Accordingly, an emphasis on consistent methodology may be unrealistic or even counter-productive. He said that estimates could be evaluated in terms of materiality. For example, a variance of 5% would be reasonable, but a variance of 50% would not be reasonable. Materiality also must consider the size of the grant accrual relative to the agency’s financial statements.

Another IPA representative said that materiality should focus on net cost rather than on the balance sheet.

A federal auditor said that at his agency, there is a problem with the “look-back” to satisfy the auditors. All of his agency’s grants are on a reimbursable basis. However, when the grantee reports come in, you don’t know whether the draw-downs that occur early in a fiscal year should be charged to the current fiscal year or a prior fiscal year.

Another federal preparer agreed and said that surveys of grantee billing cycles would be reasonable for developing an estimate. However, the new auditors decided that the agency needed to look at each grantee. However, even contacting each grantee would not reveal when the expense was incurred.
Ms. Payne noted that there were several aspects of “reasonable” estimates:

- Estimation methodology – how to choose a methodology for different programs
- The internal controls around that methodology and the look-back at the estimate
- Materiality

She said that if there is some guidance or best practices on the above, is there still a problem on the audit side?

An IPA representative said that the most helpful part of the FASAB Technical Release for credit reform\(^1\) was the concept of “best available data.” She said that the problem with SFFAS 1 and 5 is that they don’t anticipate a lack of data.

Another IPA representative noted that many auditors place too much importance on the grantee-provided data on Form 269, and that data is often cash basis, not accrual basis data. She said that some grantees do not understand accrual basis, and others do not have accounting systems that allow them to collect accrual-based data.

Another IPA representative said that some agencies accrue and then monitor. He said that it’s a good habit to check your estimates against actual.

A federal preparer agreed, and said that programs are evolving and that grantee expenditure patterns may change over time. She said that you can’t have one standard methodology because each program is so different. Many other participants indicated agreement.

A federal preparer said that it would be helpful to put SFFAS 1 and 5 into context provide clarity on what we are trying to achieve with the grant accruals. He said that with the Recovery Act we will be getting better and more timely information -10 days after the end of the quarter versus 30 to 45 days for previous grants. Even though the data is cash basis, we are trying to get a reasonable estimate.

A federal auditor said that it remains to be seen whether the reporting standards in the Recovery Act will be a bell-weather or an anomaly. She also said that there are serious concerns with the quality of the data that is coming in.

A federal preparer said that data from the grantee is the only data that agencies have in order to estimate their grant accruals.

An IPA representative said that that this is one of the dangers in this process: expending significant resources to rely on self-reported data may often be of poor quality. He said that we need to consider the wisdom of applying sophisticated procedures to poor-quality detail data.

\(^1\) For example, see FASAB’s Technical Release 6, paragraph 17.
A federal preparer said that for several years their auditors had thrown out their survey because auditors had determined that the grantees and/or the grantee sub-contractors did not really understand what they were supposed to report.

Another federal preparer said that her agency has a strong training plan – including face-to-face training for grantees- and a strong monitoring plan and that they believe that their estimate is reasonable. However, as in the credit reform estimate, all you have is the best data available\(^2\) and all you can ever get is a reasonable estimate. At the end of the day, all you can ever get is a reasonable estimate.

One federal preparer mentioned that when grantees are late reporting their funds are frozen. Other preparers said that by law they cannot do this.

An IPA representative noted that agencies need to be able to have some leverage, because otherwise if grantees can get away with late and/or inaccurate reporting, they will. He said that only Congress is able to address the leverage issue. Other participants indicated agreement. One preparer said that having a strong training programs helps, but that we need to make this process a little easier and still get a good result in terms of financial reporting.

Ms. Payne asked if this group wishes to address the monitoring process. She asked if monitoring would be within the scope of this group. Most participants indicated that this might be beyond the scope of this group. One IPA representative said that in 2004, IBM looked at the process and came up with benchmarks to see what was out there in the federal government, and came up with some best practices for monitoring. One preparer said that her agency has about 10- full-time staff doing monitoring, plus additional part-time field staff. An IPA representative observed that monitoring can pay for itself in recoveries for unallowable costs, etc. A federal preparer said that this group might talk about the impact of monitoring on the financial statements.

Ms. Payne asked if this group should address systems: for example, are there recommended changes in system requirements or any best practices regarding systems. A majority of participants indicated that this topic would be beyond the scope of this group. A preparer noted that there already are systems requirements out there and that grants activities are very variable.

**Next Steps**

**Plans for the Working Group**

Ms. Payne noted that the Task Force is too large to be a working group, and asked the group to decide whether we need more than one working group and what approach would be the most logical. She said that a couple of ideas (the question of “can you net?” and “what's the focus of materiality?”) are somewhat discrete and asked if the

\(^2\) For example, see FASAB TR 6, par. 17 re “best available data”
Attachment D: Minutes from Task Force Meeting on August 13, 2009

group would like set aside those items on a different track and then address the remaining items through a working group. The group indicated no objections.

Ms. Payne said that the remainder of the work would be something that the working group will need to put some horsepower into. For example: the notion of reasonableness in selection of estimation methodologies; and internal controls extending to a certain degree to the monitoring process, and “looking back” guidance. With this in mind, she asked whether these tasks would require multiple working groups or whether they should be viewed as a single product.

Ms. Payne said that an ideal working group would include both auditors and preparers. She asked if the working group should also include program experts. One preparer said that monitoring and oversight is done by program people so they could be consulted to review potential guidance on monitoring.

One participant asked what kind of end product is being envisioned for the working group – in particular, whether it would be part of the GAAP hierarchy. Ms. Payne said at the moment she is thinking of a Technical Release (TR) via the AACP. However, another possible venue would be staff implementation guidance (SIG). She said that the choice of an end product would be affected by the scope of the end product and how quickly the group wants to see the guidance issued. She said that due process for SIG is faster than for a TR. She said that the group may find that some things such as best practices don’t need to be in GAAP and would be best conveyed in another way. She said that FASAB staff could frame a straw-man outline for the working group but that the heavy lifting – including hands-on writing- would need to be done by the working group. She said that this time commitment should be considered by anyone volunteering for the working group and that ideally the group should have about 5 to 7 members.

Ms. Payne also asked about the timeline. She asked if the group would like to pick a fiscal year goal for the group’s work. One participant said that FY 2010 would be helpful. Ms. Payne suggested meetings in September/October and perhaps late November for the work group.

With that frame of reference, Ms. Payne asked for volunteers. The volunteers were:

Volunteers for Working Group

<table>
<thead>
<tr>
<th>Name</th>
<th>Organization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Irving, Patricia</td>
<td>HHS</td>
</tr>
<tr>
<td>Joseph, Denise</td>
<td>DJ Business Solutions</td>
</tr>
<tr>
<td>Lambert, Katherine</td>
<td>DOT/FTA</td>
</tr>
<tr>
<td>Malhotra, Shal</td>
<td>Grant Thornton</td>
</tr>
<tr>
<td>McKay, Jim</td>
<td>Kforce Gov’t Solutions</td>
</tr>
<tr>
<td>Paull, Marcia</td>
<td>DOJ/OJP</td>
</tr>
<tr>
<td>Ramos, Frank</td>
<td>DOJ</td>
</tr>
<tr>
<td>Supernaw, Cathy</td>
<td>KPMG</td>
</tr>
<tr>
<td>Thomas, Derek</td>
<td>KPMG</td>
</tr>
</tbody>
</table>
An IPA representative said that a definition for “reasonable” would be very helpful. Ms. Payne said that staff drafts on the materiality issue might provide a starting point. A federal preparer said that one challenge that came up in the roundtable is the range of legislation regarding reporting by grantees—some requirements are strict and others are lax. Because of this, the guidance may need to be flexible about reasonableness.

Ms. Payne said that due to the timing of approaching year-end, FASAB staff will try to use e-mail and teleconferencing to communicate with the Task Force as much as possible.

A federal preparer said that a major challenge is the fact that every federal grant program is different so that it is difficult to come up with guidance that would be appropriate in all cases. Other participants agreed.

Ms. Payne asked participants to e-mail Ms. Parlow with any written methodology that they have. [Note: HHS provided a hard copy of “Standard Operating Procedures: Grant Expense Accrual Calculation” dated March 5, 2008, and issued by HHS Division of Payment Management, to Ms. Parlow at the meeting.]

Ms. Parlow noted that although this project was initiated due to cost/benefit concerns, it appears that some of the discussion had indicated that aspects of the grants accrual process such as monitoring may already be cost-effective in that the results of the activities pay for themselves, or at times even more than pay for themselves, such that focusing purely on reducing costs may not be the primary goal of the group.

A federal preparer agreed, and said that for example a well-run accrual process could save money on the audit and/or other investigations. Other participants agreed.

**FASAB Discussion Points for working group meeting**

It was suggested by Task Force participants that guidance on estimation method(s) recommended by FASAB might increase the efficiency of the estimation process and ultimately reduce audit costs.

Potential implementation/technical guidance (or “best practices”) to be drafted by the working group could include:

- Adaptations of some of the FASAB TR 6 guidance for developing credit reform estimates and internal controls such as TR 6 pars. 16-22, 27-29, 31, 36, 39, 40, 41, 46 (see attached example)
- Adaptation of some of the FASAB TR 3 (Revised) guidance for auditing credit reform estimates.
- Guidance could also incorporate some or all of the JFMIP estimation methods listed in the Grants System Requirements.
Attachment D: Minutes from Task Force Meeting on August 13, 2009

- Guidance (scope) could include an exclusion of mandatory grants and why those grants are charged to expense when paid rather than included in the year-end estimate calculation.
- Draft guidance could also note that methodology might be expected to change as agencies develop experience with trends/expectations for specific grant programs.
- Decision trees (high-level) to address situations of new grant programs or programs where legislation has changed so that prior history may not be applicable for year-end estimates.

Next Steps for the Task Force

The Task Force will (a) review proposals drafted by the working group and (b) explore whether cost savings (for taxpayers) might result from netting of advances and receivables arising from grants.
Attachment: Draft Outline and Sample Guidance

Draft Outline
1. Preparing Year-End Accrual Estimates for Grant Programs
   A. Existing Programs (historical data available)
   B. New or Modified Programs (insufficient historical data available)
2. Internal Controls: Recommendations
   A. Documentation of Estimation Process
   B. Coordination with Program Managers
   C. Training Grantees
3. Materiality and Cost/Benefit Considerations

Sample Guidance
Preparing Year-End Accrual Estimates for Existing Grant Programs
1. Agencies should accumulate sufficient relevant and reliable data on which to base accrual estimates. It is important to note that agencies should prepare all estimates based upon the best available data at the time the estimates are made. 

2. Management should ensure that the following documentation is available for grant accrual estimates:
   a. Procedures used for calculating the estimates.
   b. Review and approval process for the estimate.
   c. Significant assumptions used in calculating the estimate.
   d. Historical data used to support assumptions and calculations, citing sources and timeframe
   e. Explanation of the sampling process used, including if applicable treatment of grant programs with different payment patterns, legislation, etc.
   f. Explanation of the calculation concept used, such as simple linear regression or other appropriate statistical analysis method
   g. Procedures for Error Checking
   h. Procedures for Monitoring/Validation Subsequent to fiscal year-end
ACCOUNTING AND AUDIT POLICY COMMITTEE MEETING
FINAL MINUTES
July 12, 2007

The meeting was convened at 1:00 PM in room 7C13 of the GAO Building, 441 G St., NW, Washington, DC.

ADMINISTRATIVE MATTERS

• Attendance

Present: Ms. Comes, Ms. Carrie Hug (for Ms. George), Ms. Chadwick, Ms. Healy, Messrs. Bragg, Dingbaum, David Horn (for Mr. Fletcher), McFadden, Sturgill, and Synowiec.

Absent: Mr. Campbell, Mr. Fletcher, and Ms. George

• Minutes

The minutes of May 31, 2007 were previously approved as final, having been circulated by E-mail to members.

• Administrative

None

PROJECT MATTERS

• Project Agenda Status

Inter-Entity Cost

Mr. McFadden, co-chairperson of the AAPC Inter-Entity Cost task force, gave an update on the current status of the work of the task force and the exposure draft technical release that was released for comment on June 4, 2007 and responses are due back by August 6, 2007. Mr. McFadden noted that no comment letters had been received on the exposure draft to date.

Heritage Assets and Stewardship Land

Mr. Synowiec, co-chairperson of the AAPC HA/SL task force, gave an update on the status of the exposure draft technical release that was released for comment on June 11, 2007 and responses are due back by August 13, 2007. Mr. Synowiec noted that no comment letters had been received on the exposure draft to date. Ms. Comes mentioned to the members that copies of the both exposure drafts were sent to the FASAB members to review.

• New Business

None
• Agenda Committee Report

Grant Accrual Methodologies

Ms. Comes noted that at the May meeting the AAPC’s Agenda Committee brought an issue from the Department of Transportation’s Federal Transit Administration (FTA) to the Committee concerning methodologies for calculating grant accruals. At that meeting, the AAPC did not vote to formally accept the issue as an agenda item; however the members did agree to discuss the issue again at the July AAPC meeting.

Ms. Comes noted that Ms. George had arranged to have representatives from the Department of Justice’s Office of Justice Programs (OJP) make a presentation to the AAPC on their experiences with developing grant accrual methodologies and auditor involvement. The representatives from OJP were Melinda Morgan, Director Finance Staff; Marcia Paull, CFO OJP; and Cathy Supernaw, KPMG Partner. Ms. Morgan made the introductions and gave a brief overview of the history behind OJP’s current grant accrual methodologies. Ms. Paull began her presentation by noting that OJP has approximately 14,000 grants and approximately 6,000 grantees worth $9.3 billion (2006). She continued with the following points:

- the history of OJP’s grant accruals from 2000 to 2004
- the use of a straight-line methodology
- the look-back processes
- the use of a cumulative adjustment factor
- the use of estimates and assumptions
- the continuing refinement of the accrual methodology
- the bottom line is: there is no standard way to calculate a grant accrual

Ms. Supernaw then went over some of the auditing literature governing the auditing of accounting estimates (i.e., management’s responsibilities, the auditor’s responsibilities, evaluating the reasonableness of an estimate, and the internal controls in place).

The OJP representatives then opened the discussion to questions from the AAPC members. The following are some of the questions asked by the Committee:

- Why are all 14,000 grants included in the accrual methodology instead of the use of samples? Ms. Paull replied that it was necessary to include all grants because of the varying nature of the types of grants.
- How long does it take to calculate the accrual on a quarterly basis? Ms. Paull replied that it takes three staff people three days.

After the OJP presentation, Ms. Comes mentioned to the members that after the May meeting Mr. McFadden arranged to have a brief questionnaire sent to the Financial Statement Audit Network (FSAN) members asking them about their experiences with grant accruals. The four responses received were provided to the members. Ms. Comes also mentioned to the members that the Department of Transportation had withdrawn the Federal Transit Administration (FTA) request for guidance as it relates to their grant accrual issue. Ms. Comes asked the members, based on the OJP presentation and the FSAN responses, if they wanted to accept the grant accrual issue as an AAPC agenda item. Mr. McFadden noted that based on what the Committee has heard on the issue it would be difficult to put together general guidance on grant
accrual methodologies that would be helpful to the Federal community. Mr. Sturgill noted that with the levels of complexity and varying types of grants Federal agencies are involved in it would be very hard to narrow down the methodologies into general guidance. Ms. Comes asked if any of the other members disagreed with the views of Mr. McFadden and Sturgill. None disagreed. Ms. Comes noted that based on those views the issue will not be added as an agenda item.

- Next Meeting

September 27, 2007

Adjournment: The meeting was adjourned at 1:40 PM.
1. What method does your agency use to calculate grant accrual liabilities estimation?

Grants awarded by CNCS are paid via the Payment Management System of HHS. HHS requires grantees to report their actual expenses on a quarterly basis via SF272, Federal Cash Transaction Report, which HHS issues to grantees at the end of each quarter. Since the reporting received during a given quarter applies to the grant status at the end of the prior quarter, an estimate must be prepared to recognize expense incurred by grantees since the last SF 272 date. This estimate is the grant accrual. The grant accrual is posted to Momentum at the end of each fiscal quarter and reversed in the following fiscal month. The Corporation established the grant accrual methodology for estimating the grant accrual. CNCS created this methodology to meet the earlier reporting requirements. The limitations of HHS preclude the system from producing the actual accrual until well after the November 15th deadline, therefore CNCS created this methodology to estimate the accrual as an alternative.

The grant accrual is performed on a quarterly basis using macros built into Access. The macros instruct Access to read information about individual grant accounting lines imported from Momentum. Grant lines in Momentum are summarized by purpose codes and appropriation code.

2. Does your agency have a statistically valid look-back procedure that can tie the actual payments back to the period when the costs were incurred by the grantees or grantees’ contractors, in order to validate your estimated grant accrual liabilities?

The Total Grant Accrual amount is the actual cash draw amount, which is HHS Total Quarterly Advances amount from the HHS Accrual Estimate spreadsheet. The Corporation then distributes the total grant accrual amount to grants as follows:

a. Calculates the open obligation amount for each active grant, which is the net of Total Obligation and Total Disbursement;
b. Calculates the percentage of each grant open obligation to the Total Open Obligation; and
c. Calculates the grant accrual for each grant, which is the total accrual amount multiplied by the percentage.

Grants are summarized by appropriation and purpose code for Momentum posting purposes. In determining Total Open Obligation, only appropriations that are active in the current fiscal year and not cancelled by the new fiscal year are considered.

The accrual for each individual grant is compared to the outstanding advance balance for that grant to determine if the advance should be liquidated or if the payable should be increased. For example, after processing the grant accrual, it is determined that a grantee’s accrual for a particular grant is $25,000 and the grantee has an outstanding advance for $10,000. The $10,000 will be liquidated by the accrual resulting in no remaining advance while the payable will increase by the remaining accrual, $15,000.
3. Do you have a look-back procedure that the CFO financial statements auditors have found to be acceptable for your agency? If so, would you please briefly describe the procedure?

   The Corporation’s prior external audit firm found no deficiencies in the procedure used. See above paragraphs for a description of the procedure. Presently, a different IPA firm is in its first year of a 3-year contract to audit the Corporation’s statements. It is too early to know whether the new firm will comment on this procedure.

4. What is a reasonable frequency at which to conduct a look-back analysis? Quarterly, yearly, or other? If other, please state________________.

   The analysis is performed on an irregular basis, but not less than annually.

5. If your agency does not have a look-back procedure, how do you ensure validity of your grant accrual estimation?

   Not applicable.

6. How many FTEs do you require to conduct your agency's grant accrual look-back analysis? How large is your population of grantees' payments? How large is your sample? What is the dollar value of grants for which your agency is responsible?

   The agency employs one FTE to perform the analysis. In FY06, the Corporation’s approved grant budget was approximately $834 million. The prior IPA firm applied a reasonableness standard for determining the adequacy of the accrual.
1. **What method does your agency use to calculate grant accrual liabilities estimation?**

Grants with values of $750K or less are fully costed at the time of obligation. Accruals are booked monthly for grants with uncosted balances greater than $750K using the Department’s automated accrual process. The automated accrual process computes accruals based on year-to-date payment data and the average number of days between receipt of services and receipt of invoices and posts to the general ledger at the end of each month.

2. **Does your agency have a statistically valid look-back procedure that can tie the actual payments back to the period when the costs were incurred by the grantees or grantees’ contractors, in order to validate your estimated grant accrual liabilities?**

Yes, accruals for all grants greater than $750K are reviewed at least annually as a part of the Department’s “true-up” process to ensure that accruals reflect actual costs.

3. **Do you have a look-back procedure that the CFO financial statements auditors have found to be acceptable for your agency? If so, would you please briefly describe the procedure?**

At least annually, the Department compares payment requests submitted by grantees (invoices) to recorded costs for all grants greater than $750K, researches the differences and makes adjustments to correct the accounting records.

4. **What is a reasonable frequency at which to conduct a look-back analysis?**

Quarterly, yearly, or other? If other, please state________________.

Yearly. (Chicago has about half of the grants and does it at 6/30 and 9/30 each year)

5. **If your agency does not have a look-back procedure, how do you ensure validity of your grant accrual estimation?**

N/A

6. **How many FTEs do you require to conduct your agency's grant accrual look-back analysis? How large is your population of grantees’ payments? How large is your sample? What is the dollar value of grants for which your agency is responsible?**

During Fiscal Year 2006 there were approximately 61,000 payments to grantees totaling $1.3B. During Fiscal Year 2006 approximately 92% of the active awards should have been covered by the annual “true-up” process. The Department requires about .5 FTE for
the true up process. Determining the total value of grants would be difficult but the total amount obligated in a given year is approximately $1.5B
1. What method does your agency use to calculate grant accrual liabilities estimation?

Grant costs are required to be reported by grantees quarterly. Each quarter’s reports are entered into our accounting system with the date of the quarter being reported. Each grant payment is tagged with the date of the draw.

DOL/ETA uses grant payments at the end of the period to estimate actual costs and then accrues for any difference between estimated and reported/recorded costs.

2. Does your agency have a statistically valid look-back procedure that can tie the actual payments back to the period when the costs were incurred by the grantees or grantees’ contractors, in order to validate your estimated grant accrual liabilities?

Because our costs and payments are dated when submitted, we do not need to “tie the actual payments back to the period when the costs were incurred”. However, because our cost reports come in after the quarterly and annual financial statements are due, we must accrue for expected costs at the end of the period. Our look-back procedure evaluates the overall accuracy of our accrual procedure versus actual costs reported after year end.

3. Do you have a look-back procedure that the CFO financial statements auditors have found to be acceptable for your agency? If so, would you please briefly describe the procedure?

Accrual accuracy is validated by tracking the cost reports received during the next year, updating the accrual database for prior year costs reported after year-end, and comparing the accrued costs to the actual costs reported. We test all grants for which later data is available, usually about 85% of the accrued grant costs. This is not statistically valid, but statistical sampling is not efficient since a cost report is not necessarily received for each grant accrued for and thus the sample may be compromised.

4. What is a reasonable frequency at which to conduct a look-back analysis? Quarterly, yearly, or other? If other, please state________________.

Annually

5. If your agency does not have a look-back procedure, how do you ensure validity of your grant accrual estimation?

N/A
6. How many FTEs do you require to conduct your agency's grant accrual look-back analysis? How large is your population of grantees’ payments? How large is your sample? What is the dollar value of grants for which your agency is responsible?

The accrual process and the accuracy analysis are heavily automated using MS Access and Excel, with the ability to post entries to the accounting system using bulk files generated by Access. Currently producing and posting quarterly accruals uses about 10 staff hours per quarter and involves mostly senior accountants and accounting database administrators (GS-14).

The annual accuracy analysis data generation is mostly automated, and takes about 10 hours of senior accountant effort to produce the standard analysis and documentation. If the analysis indicates possible problems or changing conditions, trouble-shooting can be very time consuming.

Our process was developed by contractors from 1994 to 1996 and involved approximately 1 staff year spread over that time frame.

ETA has:

90 K payment transactions per year
About 4,500 active grants each year
$9.5 billion in grant funding per year
NASA OIG
Federal Transit Administration’s Grant Accrual Methodology and Look-back Procedure
Questions for FSAN

1. What method does your agency use to calculate grant accrual liabilities estimation?

   NASA does not calculate a grant accrual. The lack of a grant accrual is listed as an issue within the Financial Systems, Analyses, and Oversight material weakness in our current IPA’s last 3 Reports on Internal Control (i.e., FY 2004 – 2006).

2. Does your agency have a statistically valid look-back procedure that can tie the actual payments back to the period when the costs were incurred by the grantees or grantees’ contractors, in order to validate your estimated grant accrual liabilities?

   N/A

3. Do you have a look-back procedure that the CFO financial statements auditors have found to be acceptable for your agency? If so, would you please briefly describe the procedure?

   N/A

4. What is a reasonable frequency at which to conduct a look-back analysis? Quarterly, yearly, or other? If other, please state________________.

   In my opinion, a reasonable frequency would be yearly, at a minimum. However, the frequency of the estimation of the grant accrual may affect the frequency of the look-back analysis.

5. If your agency does not have a look-back procedure, how do you ensure validity of your grant accrual estimation?

   NASA does not calculate a grant accrual.

6. How many FTEs do you require to conduct your agency's grant accrual look-back analysis? How large is your population of grantees’ payments? How large is your sample? What is the dollar value of grants for which your agency is responsible?

   N/A