# Issue

Inconsistency among services on how capital project funding is held prior to the project pay out (restricted vs. equity). Since this issue was discussed verbally at early Working Group meetings, each Service’s precise positions and concerns were not available and thus are not documented. However, it was noted that the Services had verbally concurred with the recommendations at the time of these discussions in 2014.

# Research

Below outlines the current treatment of how each service complies and what the regulations, accounting guidance and industry standards are for this area.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Capital Project Accounting Guidelines | Air Force | Army | Navy | Marines |
| DoDI 1015.10 and DoDI 1015.15: Silent on treatment | N/A | N/A | N/A | N/A |
| FMR Volume 4, Chapter 1. 010303. Restricted Cash:  Restrictions are usually imposed on cash deposits by law, regulation, or agreement.  Nonentity cash is always restricted cash. Entity cash may be restricted for specific purposes. Such cash may be in escrow or other special accounts. Financial reports should disclose the reasons and nature of restrictions. | Unclear | Unclear | Unclear | Unclear |
| GAAP: ASC 350-10  Summary of Restricted and Designated Funds:  Cash and cash equivalents disclosed on the balance sheet should agree to the amount disclosed in the statement of cash flows. Accordingly, when restricted cash is presented separately in the balance sheet, it should not be included in cash and cash equivalents in the statement of cash flows.  From time to time, an entity may designate or appropriate unrestricted funds for specified purposes, such as capital improvements or long-term investments. Although segregation or disclosure of these designated funds is not required, such action is acceptable so long as the disclosure does not imply that the funds are legally restricted. If such funds are to be used to acquire noncurrent assets, liquidate long-term debt, or purchase long-term investments, they should be classified as long term.  Significant amounts of funds that are legally restricted in other ways should also be segregated or disclosed in a caption or note. Funds held in escrow, proceeds from loans restricted for specified purposes, and reserve funds required under bond indentures are examples of such funds. If such funds are to be used to acquire noncurrent assets or to liquidate long-term liabilities, they should be classified as long term in a classified balance sheet. However, if funds are restricted for the payment of interest, current maturities of debt, or other current liabilities, they should be classified as current.  In SEC filings, registrants are required to separately disclose on the face of the balance sheet any cash or cash items that are legally restricted as to usage or withdrawal, and the terms of the restrictions must be described in a note to the statement. | Unclear | Unclear | Unclear | Unclear |
| FASAB Handbook version 12: Silent on treatment | N/A | N/A | N/A | N/A |
| Industry Practice: If funds are legally restricted towards a use, then companies use restricted fund accounts. However, if there is no legal restriction, insufficient cash on hand but sufficient income, or a desire to not reduce the cash balance, companies may place the reserve in the equity section of the financial statements. | N/A | N/A | N/A | N/A |

# Discussion

Since the reserve in question is for the acquisition of an asset rather than as an accrual for a future liability (which must go into the equity section), there is a degree of flexibility for Services setting aside funds for future acquisitions. Legally restricted funds should always be in the restricted cash section, per the FMR and GAAP guidance. Funds that are not legally restricted may be either 1) recorded as unrestricted reserved for assets intended to be purchased in over a year (noncurrent to match the asset intended to be acquired with clarification that the funds are not legally restricted) and as a subaccount of cash for assets to be purchased within the year, 2) in the cash account, or 3) as an equity account via storage as an equity account with a corresponding reduction in Retained earnings. Option 1 will negatively impact the liquidity metrics of the reporting entity, as current assets, specifically cash, will decrease and noncurrent assets will increase with these discretionary reservations.

Option 2 maintains the same liquidity metrics. The reporting entity could keep the funds reserved for a future project (reserved by discretion, not reserved legally) within the cash account.

The third option reduces Retained Earnings by the reserve account, but maintains the cash balance and liquidity measures.

Provided the funds are not legally restricted, the choice between the three methods is one of preference.

# Recommendation

We recommend that the Services use the restricted cash account (GLAC 107 Restricted Cash) for legally restricted funds only. Legally restricted cash must be disclosed as such. Additionally, the Services should place funds that are set aside for future capital purchases or projects but are not legally required to be spent in a separate account. We recommend the addition of GLAC 108 “Capital Projects Reserve” for this purpose; however, the Services are not required to separate and disclose funds held for capital projects that are not legally restricted. We recognize that GAAP and the FMR do not prescribe this distinction; however, with the expectation that NAFIs by their nature will have numerous capital projects and many projects with legally restricted cash, we believe this to be the best method to ensure comparability between the Services. Without a standard approach, meaningful comparisons between the Services’ cash balances, financial ratios, and retained earnings will be difficult to achieve, particularly in times with numerous capital projects.

We recommend the FMR Volume 4, Chapter 1 be changed to include this distinction in accounting treatment between legally-restricted cash reserves and voluntary reserves. Recommend including the following statements within the FMR: “Legally-restricted cash should be held separately from non-legally restricted cash and disclosed as such within the financials. Although cash set aside as a reserve for non-legally restricted purposes such as projects may be segregated from Cash, it is not required to be segregated. Additionally, any disclosures related to reserves should not imply that the funds are legally-restricted.”

Also, we recommend the NAFSGL (Chart of Accounts) be updated to define Restricted Cash as a legally-restricted asset account and Capital Projects Reserve as an optional reserve account for capital project funds that are not legally restricted.

# Service Concurrence

|  |  |  |
| --- | --- | --- |
| Service | Concurrence | Reason for Non-concurrence |
| Air Force | Concurrence in 2014.**Re-concurred 10/19/2018.** |  |
| Army | Concurrence in 2014. **Re-concurred 11/2/2018.** |  |
| Marines | Concurrence in 2014. **Re-concurred 1/8/2019.** |  |
| Navy | Concurrence in 2014. **Re-concurred 6/21/2019.** |  |

# USD(P&R)/MC&FP Disposition

Revise the NAFSGL.

**DFAS Disposition**

Revise DoD FMR Volume 4, Chapter 1.

# Forward to DoDIG?

No DoDIG equities.