# Issue

Based on one on one discussions held with each of the Services and analysis of the Program Metric Report, Grant Thornton has noted differences among the Services in application of the NAFSGL Chart of accounts and approach to filling out the Program Metric Report. While the full extent of differences is not fully known, the noted differences significantly impact the comparability of the financials between the Services.

# Research

Below outlines the position on the reporting of Sales versus Other Operating Revenue by Service.

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| Sales vs Other Operating Revenue Treatment and Guidance | Air Force | Army | Marines | Navy |
| NAFSGL 3.0 Definitions:  400: Gross Sales Revenue: All sales, including sales of goods and services central to an entity’s ongoing major or central operation, within the fiscal year. Goods must have been delivered to the customer, and services must have been performed before sales revenue can be recognized. (Source: GAAP, FMR) | Does Not Follow: Reports revenues from goods as sales, and revenue from services/participation as Other Operating Revenue | Unclear:  Revenue generated without Cost of Goods Sold is considered a service fee instead of a sale. | Does Not Follow:  Sales classification largely depends on Funding Category. Most Category C services are considered Sales. All Category B (except tickets) are considered Other Operating Revenue. | Unclear:  Navy tends towards heavy usage of Other Operating Revenue in all categories. |
| NAFSGL 1.0 Definition  403: Participation Fee Revenue  Revenue from fees charged to customers for participating in programs, such as but not limited to athletic events, special events, golf green fees, bowling leagues, lodging room nights, etc. (Source: FMR) | Unclear where currently reported in PM report | Unclear where currently reported in PM report | Unclear where currently reported in PM report | Unclear where currently reported in PM report |
| NAFSGL 1.0 Definition  412: Other Operating Revenue:  Revenue that does not fit any other GLAC income category. (Source: GAAP) | Does Not Follow:  Revenue earned from offering Services (i.e., a round of golf or bowling).  Cost of providing services captured in a variety of expense accounts | Does Not Follow:  Size of account exceeds Gross Sales by a 2 to 1 margin. By definition, Gross Sales should be the largest stream of revenue reported | Does Not Follow:  Classification depends on Funding Category. Most Category B’s use Other Operating Revenue. Category C’s use a small amount for commissions and rental revenue | Does Not Follow  Size of account slightly exceeds Gross Sales. By definition, Gross Sales should be the largest stream of revenue reported |
| NAFSGL 2.0 Definition  502: Cost of Goods Sold  Cost paid for merchandise sold. Cost of Goods Sold includes the cost of freight deemed to be material and readily assignable to individual inventory items or items transferred from other cost centers. This GLAC is to be used in conjunction with the perpetual inventory accounting method.  (NOTE: Was not present in NAFSGL 1.0)  No Cost of Sales/Services in NAFSGL | Follows Guidance:  Cost of Goods sold, as currently structured, is only for inventory goods. Assumes no variable costs in earning service/ participation revenue | Follows Guidance:  Cost of Goods sold, as currently structured, is only for inventory goods. Assumes no variable costs in earning service/ participation revenue | Follows Guidance:  Cost of Goods sold, as currently structured, is only for inventory goods. Assumes no variable costs in earning service/ participation revenue | Unclear |
| Additional Notes | N/A | N/A | Since Category B is subsidized, and the intention of category B is not strictly profit, the money earned from Category B programs is considered Other Operating. ITT is considered an exception.  Sales, whether of goods or products, in Category C programs do not require a cost of goods sold. | Navy’s one on one meeting was held before this issue was known. |

# Discussion

In order for the Service programs to be reasonably comparable between Services, the following issues must be addressed:

1. The purpose of the 400: Gross Sales account. Consistent with GAAP and general industry practice, the Sales due to core operations, whether they be services or goods, are intended to be the primary source of revenue and hence a primary indicator of performance.
2. The purpose of the 403: Participation Revenue account. This is an FMR based account.
3. The issue of Cost of Goods Sold reflecting an inventory-based business, while many of the MWR programs are service-oriented.

# Recommendation

1. Based on the Working Group meeting held on September 20, 2018, the Working Group determined that the status quo of the account definitions was not workable due to the conflation of revenue from services provided and revenue from goods sold being intermixed in the Sales account, while the service revenue could also be included in the Participation fee account. Analysis of the Program Metric Report further confirmed that the lack of clear demarcation between these accounts led to unclear financial reporting. Grant Thornton proposed a series of potential solutions to resolve this issue, and the Working decided upon the following changes to the NAFSGL and related policy:

* The Gross Sales Account (currently 400) will be changed to Revenue from Goods Sold and the definition will be adjusted to only include sales revenue from sale of goods, both physical and electronic goods.
* The Participation Fee Revenue Account (currently 403) will be changed to Revenue from Services Provided. The definition will be adjusted to include the reporting of revenue from services provided and participation fee revenue earned by providing an activity to a service member irrespective of how the Services record the revenues internally. The Services have the option to record revenue from services separately from participation fee revenue internally as long as both amounts are included in the Revenue from Services Provided GLAC for OSD reporting purposes.
* The Cost of Goods Sold (currently 502) account will remain the same; only including the cost of inventoriable goods sold. Gross margin figures will be determined by subtracting Cost of Goods Sold from the Revenue from Goods Sold account.
* There will not be a Cost of Services Provided GLAC because the Services determined that the cost structure for the program earning revenue from Services provided is predominantly fixed in nature, and therefore a variable cost GLAC is not needed. Grant Thornton further adds that the implementation of such an account would likely lead to inconsistent practices and may compromise the comparability of other expense accounts.

1. Additionally, Grant Thornton recommends that OSD and Grant Thornton work together to implement the above instructions ahead of the Program Metric Report. The Program Metric Instructions may need to be changed to reflect the above decisions, and properly categorize types of revenue.
2. This paper will require adjustment to the FMR and the NAFSGL.

# Service Concurrence

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| Service | Concurrence | Reason for Non-concurrence |
| Air Force | **Concurred 11/15/2018.** |  |
| Army | **Concurred 11/15/2018.** |  |
| Marines | **Concurred 1/8/2019.** |  |
| Navy | **Concurred 11/15/2018.** |  |

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

No further action.

# DFAS Disposition

Revise FMR to reflect account changes listed above, particularly the distinguishment between the revenue accounts and COGS account.

# Forward to DoDIG?

No DoDIG equities.