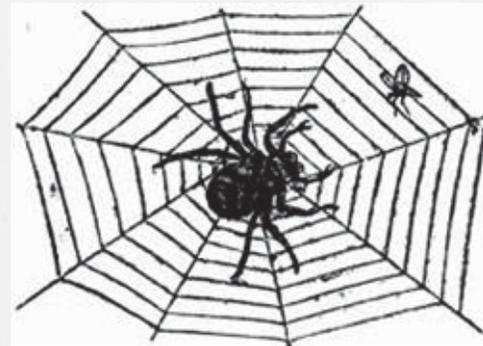


Obligations and Cobwebs



Ed Martin

What is an obligation?

- o A concept we are all familiar with
- o Spending money is something we all do
- o What does “spend” mean?
- o There are two components:
 - o Promising to pay – the obligation
 - o Paying – the outlay

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An obligation is:

A legally binding agreement that will result in outlays, immediately or in the future.

An outlay is:

A payment to liquidate an obligation.

Why is this concept important?

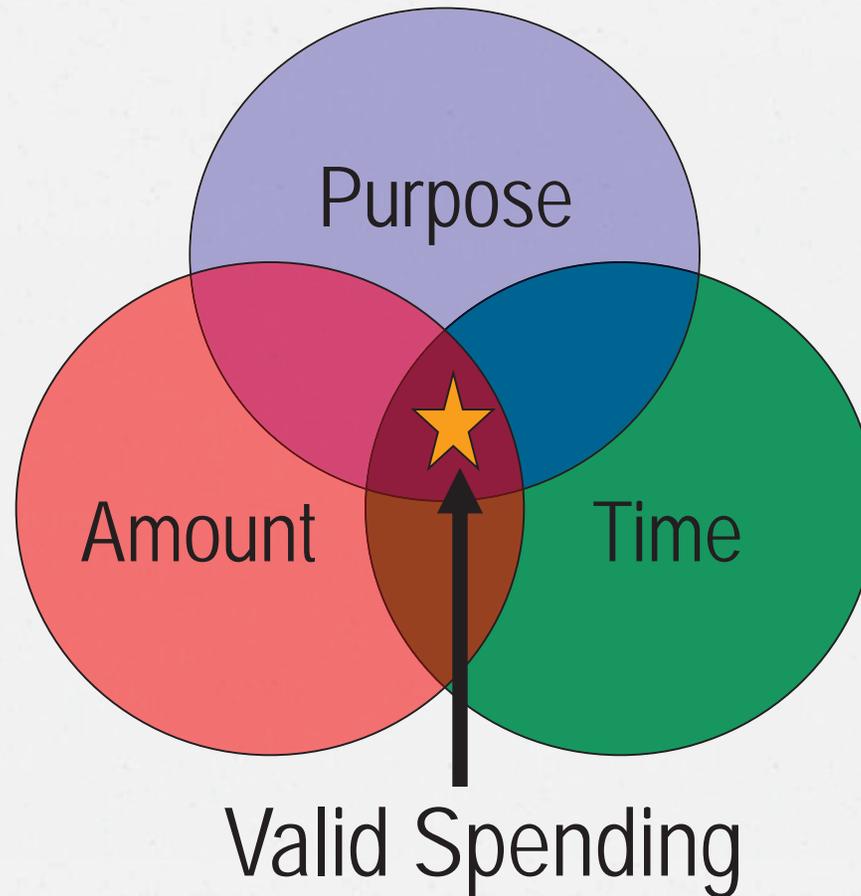
What is an obligation?

- o The “obligation” – or promise to pay - is the initial action in the Federal spending process
- o Appropriations laws establish whether funds are available to obligate
- o The concept of obligation is central to appropriations law

Appropriations Law Context

- o A valid obligation must follow the principles of appropriations law
 - o Spend only for **purposes** authorized by law (31 USC 1301)
 - o Don't spend more than the **amount** appropriated or before it is appropriated (31 USC 1341)
 - o Spend only during **time** period provided for a *Bona Fide* need of that time period (31 USC 1502)

Appropriations Law Context



What is needed to Obligate?

- o A budgetary resource (31 USC §1341(a))
- o A funds control process
 - o Apportionment (31 USC §1517)
 - o Allotment/Allowance (31 USC §1514)
- o Documentary evidence (31 USC §1501)

Why Documentary evidence?

- o Before 1954:
 - o No uniform meaning of obligation
 - o Agencies recorded “bogus” obligations where none existed to keep funds from lapsing
 - o Appropriations Committees could not obtain reliable obligation amounts
 - o Actual agency needs not clear

- o Led to passage of the “Recording Statute” - section 1311, Supplemental Appropriations Act, 1955 – codified at 31 USC §1501
- o Established standards for proper recording of obligations
- o Ensures that agencies record only those transactions which meet specified standards for legitimate obligations

What are the Standards?

31 U.S.C. 1501 requires documentary evidence of :

- o a binding agreement between an agency and another person (including an agency), that is, a **contract**
- o a **loan agreement** showing the amount and terms of repayment
- o an **order** required by law to be placed with an agency
- o an **order** issued under a law authorizing purchases without advertising
- o a **grant or subsidy**

- o a liability that may result from **pending litigation**
- o **employment or services of persons or expenses of travel** under law
- o services provided **by public utilities**
- o **other legal liability** of the Government against an available appropriation or fund.

Must you Record an Obligation?

- o If any of the previous criteria are met, the agency **must** record the transaction as an obligation
- o Recording provides evidence of the obligation, but **does not** create it
- o If a transaction doesn't meet one of the previous criteria, recording will not make it valid
- o Failing to record a valid obligation does not diminish its validity or change the FY to which it is properly chargeable

Nuances

- A. The general rule
- B. Personnel compensation and benefits
- C. Contractual services and supplies
- D. Intragovernmental services and supplies

A. General Rule

- o An obligation may be “matured” or “unmatured”
 - o “Matured” means a liability that is currently payable
 - o “Unmatured” means a liability that is not “currently payable” but for which a definite liability exists in the future
- o Examples:
 - o The Corporation for National and Community Service incurred an obligation for AmeriCorps educational benefits at the time it entered into grant agreements to provide educational benefits after successful program completion (B-300480)
 - o DoD incurred an obligation for an entire retention bonus at time of agreement – even if paid in installments (B-325526)

B. Personnel compensation and benefits

- **Amount** is prescribed by laws that cover the civil service and the uniformed service and determined by well-established personnel procedures
- **Timing** - amounts generally are recorded as obligations as the amounts are earned during the reporting pay period, with some exceptions:

- o **Severance pay** is obligated at the time paid on a pay period by pay period basis
 - o Because it is not earned with regular salaries and wages
- o **Expenses incident to relocation** - Authorized reimbursable expenses estimated to be paid to employees for real estate, temporary subsistence, etc., at the request of the Government is obligated when the individual orders are approved
 - o Because a *bona fide* need doesn't exist until the order is approved

- o **Cash awards** (not part of the employee's basic rate of pay), **allowances for uniforms and quarters**, and **subsidies for commuting costs** are obligated when payable to the employee
 - o Because this is the time the amount is definite
- o **Unemployment compensation** payments to the Department of Labor for former employees are obligated when the agency receives the bills rendered by Labor
 - o Because of the underlying law

- o **Annual leave** is obligated when it becomes due and payable as terminal leave or taken in lieu of a lump sum payment
 - o Because annual leave is normally unfunded
- o Business-type revolving fund operations that fund annual leave obligate and pay annual leave when employees are transferred
 - o To the receiving account if another revolving fund
 - o To the general fund if a non-revolving fund

C. Contractual services & supplies

- Services and supplies that are purchased by contract are recorded as obligations at the time there is a **binding agreement**- usually when the contract is signed.
- As a general rule, the amount of the obligation is the **maximum liability** to the Federal Government
- The maximum liability is normally limited by the terms of the contract (e.g., cancellation clauses)
- Nuances for certain types of contracts:

- o Contracts with a maximum price - the amount obligated is the maximum price at the time the contract is signed
- o The amount is adjusted downward (deobligated) when there is documentary evidence that the price is reduced

- o Letters of Intent and letter contracts - normally no amount is obligated at the time the letter is signed
- o However, if the letter constitutes a binding agreement under which the contractor is authorized to proceed -
- o The maximum amount indicated in the letter is obligated at the time the letter is signed

- o For Blanket Purchasing Agreements (BPAs) or Basic Ordering Agreements (BOAs), no obligation is required
 - o For contracts for variable quantities (like IDIQs) followed by “purchase orders” - usually only a “guaranteed minimum” is obligated at the time the contract is signed
 - o When a purchase order follows - the amount of the purchase order is obligated when issued
- o Most other types of orders are obligated for the amount of the order when the order is issued

Bona Fide Need Rule

- o Annual appropriations are available only to meet *bona fide* needs of the fiscal year for which they were appropriated
- o You cannot use this year's appropriations for the needs of the next fiscal year
- o The Bona Fide Need rule does not apply to no-year appropriations - only to fixed-period appropriations (annual & multi-year)

- o When the government purchases **goods or materials** in one fiscal year and they are delivered in the next fiscal year, how does this contract meet the *bona fide* need rule?
 - o “Lead time” exception
 - o “Stock level” exception

- o When the government purchases **services** in one fiscal year and they are delivered in the next fiscal year, how does this contract meet the *bona fide* need rule?
- o Must first determine whether contract is for services that are:
 - o Non-severable or entire
 - o Severable

Severable versus Non-Severable

- o A contract is considered “non-severable” or “entire” if it represents a single undertaking, even if it extends over more than one fiscal year
- o Examples:
 - o A contract for the cultivation and protection of a tract of rubber-bearing plants, payable upon completion of the services
 - o A research contract, payable upon a final report
- o Obligations are charged to the fiscal year in which the contract is signed

- o A contract is considered “severable” if the services are continuing and recurring in nature
- o Examples:
 - o Personal services
 - o Window cleaning
- o Obligations for severable service contracts may only cover the period of availability of the obligating account (usually one year)
- o The Federal Acquisition Streamlining Act permits such one-year contracts to span two fiscal years

- o The terms “severability” and “non-severability” refer to **services**
 - o Generally do not apply to grants
 - o Contracts acquire goods and services
 - o Grants provide financial assistance
- o A *bona fide* need analysis of grants focuses on:
 - o Whether the grant was made during the POA of the appropriation charged
 - o Whether the grant furthers the authorized purpose of the program

D. Intragovernmental services and supplies

- o Obligating rules are based on the statutory authority that governs the transaction
- o Economy Act (generic authority)
 - o The agreement is recorded as an obligation by the ordering agency at the time the agency enters into a “binding agreement”
 - o If ordering agency has fixed-year funding, they must de-obligate to the extent performing agency has not incurred an obligation

- o Non-Economy Act (specific authority)
 - o E.g., Government Employees Training Act, Federal Supply Schedule, Government-wide Acquisition Contracts, Stafford Act
 - o The agreement is recorded as an obligation by the ordering agency at the time the agency enters into a “binding agreement”
 - o No deobligation requirement
- o Stock orders
 - o Are recorded as obligations if it is a *Bona Fide* need of year ordered or replacing stock and if the order is firm and complete
 - o If out of stock, not a recordable obligation

o Revolving Funds

- o Special exceptions to the general rule that Congress appropriates funds for an agency's use on a fiscal-year basis
- o However, obligations to a revolving fund must meet the 31 USC 1532 test:
 - o “Except as specifically provided by law, an amount authorized to be withdrawn and credited is available for the same purpose and subject to the same limitations provided by the law appropriating the amount.”

- o Payments to a revolving fund become “no-year” only if they are earned by the revolving fund either:
 - o As costs of operating the program (“accounting services and administrative costs”) or
 - o By performing a service
- o Unobligated balances do not automatically become “no-year” by virtue of transfer to the no-year revolving fund
- o See FEDLINK opinion (B-288142)

Other Requirements

- Statutory Requirement for Certification
- OMB Requirement for Certification
- System Requirement
- Obligation Accounting

Statutory requirement for certifying obligations

31 USC §1108(c)

- o The head of an agency shall include with an appropriation request submitted to the President a report that the statement of obligations submitted with the request contains obligations consistent with section 1501 of this title.
- o The head of the agency shall support the report with a certification of the consistency and shall support the certification with records showing that the amounts have been obligated.

- o The head of the agency shall designate officials to make the certifications, and those officials may not delegate the duty to make the certifications.
- o The certifications and records shall be kept in the agency—
 - o in a form that makes audits and reconciliations easy; and
 - o for a period necessary to carry out audits and reconciliations.

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Requirement for Certification

- When year-end GTAS information is submitted, the information must:
 - Pass GTAS edit-checks
 - Be certified correct by a “certifier” separate from the “preparer” (i.e. data entry person)
- In addition, GAO requires your auditors to determine:
 - Whether controls exist to ensure that the amounts in your systems and the amounts submitted via GTAS agree. See GAO-02-126G "Guide for Auditing the Statement of Budgetary Resources".

System Requirement

31 USC §1514. Administrative division of apportionments

- o The official having administrative control of an appropriation...shall prescribe by regulation a system of administrative control not inconsistent with accounting procedures prescribed under law. The system shall be designed to-
 - o restrict **obligations** or expenditures from each appropriation to the amount of apportionments or reappropriations of the appropriation; and
 - o enable the official or the head of the executive agency to fix responsibility for **an obligation** or expenditure exceeding an apportionment or reappropriation.

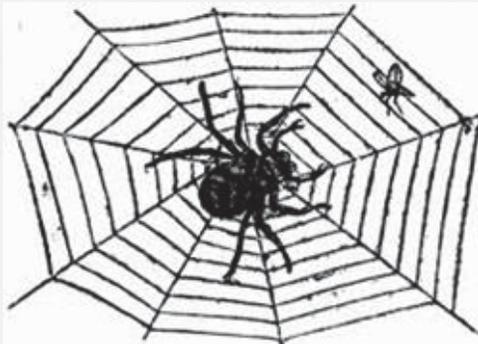
Obligation Accounting

- o The concept of ensuring valid obligations requires “budgetary” or “fund” accounting
- o Entirely different set of accounts from proprietary accounting
- o Provides a record by which federal expenditures may be traced back to the budgetary authority granted by Congress through appropriations

Obligation Accounting

- o For budgetary purposes, obligations may be classified by SGL account as:
 - o Undelivered, unpaid
 - o Undelivered, pre-paid
 - o Delivered, unpaid
 - o Delivered, paid
- o And by attribute as:
 - o Direct or reimbursable
 - o Discretionary or mandatory

Cobwebs



Cobwebs

- o Services Contracts – be very careful in determining whether a contract is severable or non-severable
- o Do not incrementally fund non-severable contracts
- o Do not forward fund severable contracts
- o Beware of indemnification!
- o E.g., “Terms of Service” agreements for social media (OLC opinion 3/27/2012)



Cobwebs

- o Monitor your obligated balances or “undelivered orders (UDOs)”
- o You have 5 fiscal years after the appropriation expires to pay/adjust obligations - then funds are cancelled
- o Bills received after pay cancellation are paid out of your unexpired appropriation
- o Watch your contracts with incentive clauses
- o You may need recovered resources to cover subsequent adjustments

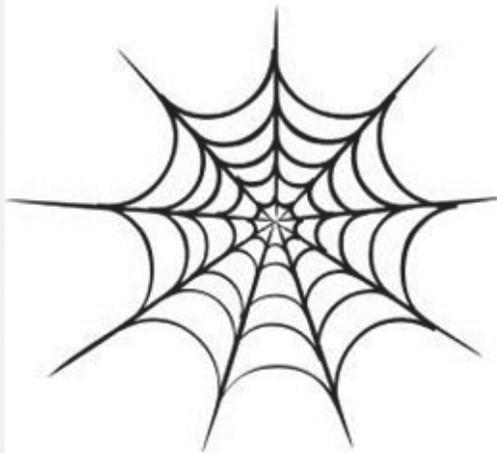


Cobwebs

- o Know your appropriation law statutes:
 - o Anti-Deficiency Act
 - o Purpose Statute
 - o Bona Fide Need Rule
 - o Recording Statute
- o Make sure obligations meet basic requirements of purpose, amount, and time
- o Use your accounting system to establish proper controls



Questions?



Disclaimer

- o This presentation cannot substitute for the application by the Office of the General Counsel (OGC) of appropriations law to the facts and circumstances of a particular situation and should not be used as the sole basis for decision-making.
- o If there is any question concerning the application of appropriations law, you must seek the advice of your agency's OGC.