DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

June 10, 2013

OFFICE OF
INSPECTOR GENERAL

OIG-13-CA-008

Walter W. Harsch, C.P.M.
2474 E Hilbar Lane
Green Valley, Arizona 85614

Dear Mr. Harsch:

On behalf of Inspector General Thorson, I am responding to your letter dated January 18, 2013, regarding two concerns you expressed with the Effective Annual Discount Rate (EADR) formula below that is included in the *Treasury Financial Manual, Volume1, Part 6, Chapter 8000 Cash Management, Section 8040.40 – Cash Discounts (TFM)*.

$$\frac{\text{Discount Percent}}{\text{100 Percent Minus Discount Percent}} \times \frac{\text{Annual Calendar Days (360)}}{\text{Number of Days in Payment Period} \; (-) \; \text{Number of Days Left in Discount Period}} = \textbf{Effective Annual Discount Rate (EADR)}$$

(Factor 1) **(Factor 2)**

Your first concern was with the denominator in Factor 2 of the EADR formula, which is the difference between two components – *Number of Days in Payment Period* and *Number of Days Left in Discount Period*. In your letter, you proposed that the dominator should be the difference between the *Number of Days in Payment Period* and the number of elapsed days between the date of the invoice and the date of its receipt by the government.

Consistent with 5 CFR Part 1315 Prompt Payment, the payment period in the EADR formula generally begins with the date of receipt of an invoice. The *Number of Days Left in Discount Period* of the EADR formula represents the government's available discount period, that is, the number of days of the payment period that the government has the ability to take advantage of the discount once it receives an invoice. In this regard, the discount period in the EADR formula begins with the date of an invoice. However, since the payment period for the EADR formula begins with the date of receipt of the invoice, the discount period is reduced for the days elapsed since the date of the invoice to the beginning of the payment period to determine the discount period available to the government.

We discussed your concerns with Bureau of the Fiscal Service staff, the Department of the Treasury organization responsible for the TFM, and they believe that the EADR formula in the TFM is correct. In addition, as part of our research, we consulted with the Chair of the Department of Accounting and Information Assurance of the Robert H. Smith School of Business at the University of Maryland, who also believes that the EADR formula is correct. Based on our analysis and discussions, we conclude that the EADR formula is correct as presented in the TFM.

Your second concern involved the use of 360 annual calendar days instead of 365 days to compute the EADR. The use of 360 annual calendar days is consistent with accepted commercial practice to simplify interest computations. It is also consistent with the annual days used to calculate interest in federal regulations, such as 5 CFR Part 1315 Prompt Payment. Accordingly, we conclude that the use of 360 annual calendar days in the EADR formula is appropriate and reasonable.

In closing, we do want to thank you for bringing this matter to our attention. I hope this information above is helpful.

Sincerely,

/s/
Marla A. Freedman
Assistant Inspector General for Audit