

FILE NO. 705 / 20

THE TEARDOWN

The \$X Rebate Surprise

\$X is the rebate swing already sitting in your accruals — the one you won't see until it lands. This teardown reconstructs, line by line, exactly how one gets built (for the finance team inside, X came to \$160,000, surfaced in a single Q4 true-up) — and the governed version that never surprises anyone. The only open question is the size of yours.

PREPARED BY



TWO DECADES ARCHITECTING OFF-INVOICE & REBATE SYSTEMS AT FORTUNE-500 SCALE

SECTION 01 — HOW TO READ THIS TEARDOWN

A reconstruction, not a horror story

This is an illustrative reconstruction of a failure pattern we see in nearly every spreadsheet-run rebate program — numbers changed, the mechanics exact. Nobody here was careless. The accrual was booked every month, tied to a real contract, by someone who knew the accounting. It broke anyway, because the method had four quiet assumptions in it. Each is tagged below.

THE SETUP The program and how the team accrued it.

WHY The assumption underneath it — usually invisible.

WHERE IT BROKE The specific point the number went wrong.

DEFENSIBLE What the governed version does instead.

THE PROGRAM

One customer. A retroactive volume tier.

TIER 1 · TO \$10M 2% Rebate on all qualifying purchases up to \$10M in the calendar year.	TIER 2 · \$10M–\$12M 2.5% Applied to the band, as volume climbs through it.	TIER 3 · ABOVE \$12M 3% · retro Retroactive to dollar one. Cross \$12M and the 3% rate reprices the <i>entire</i> year, not just the top band.
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The team accrued monthly at **2%** against the budgeted full-year volume of **\$9.8M** — the customer had landed just under \$10M three years running. By November the accrual stood at roughly **\$200K**. Reasonable. Defensible-looking. Wrong.

SECTION 02 — WHERE THE NUMBER WENT WRONG

Four assumptions, one Q4 swing

- 1 · In H2, the customer's orders accelerated — a new distribution center, more SKUs. By early December, actual purchases were tracking to **\$12.4M**, not \$9.8M.
- 2 · Crossing \$12M triggered the 3% rate **retroactive to dollar one**. The rebate owed was no longer 2% of \$9.8M (~\$196K). It was 3% of \$12.4M — **\$372K**.
- 3 · The accrual had been built at 2% against budget and never re-based to where volume was actually heading. The entire gap — **~\$160K** — landed in a single Q4 true-up.
- 4 · When the controller was asked to explain the swing, the number lived in a workbook only she could run. Reconstructing how each month's figure had been derived took three days.

WHY

Accrued against budget, not a live re-forecast. Last year's landing spot was treated as this year's destination. The method had no way to see the customer climbing toward the cliff.

WHERE IT BROKE

The retroactive tier wasn't modeled as a step. A retro-to-dollar-one tier is a cliff, not a slope — the whole year reprices at once. A flat 2% line can't represent it, so nothing was reserved for the catch-up.

WHERE IT BROKE

The estimate was never re-based. ASC 705-20 expects a change in estimate each period as expectations move. Held flat, the correction has nowhere to go but one lumpy quarter — exactly the swing a CFO never wants to hear about in December.

WHERE IT BROKE

The number wasn't reconstructable. If you can't show how a prior accrual was derived, on demand, you can't defend it to an auditor or explain it to a board — you can only apologize for it.

SECTION 03 — THE VERSION THAT NEVER SURPRISES ANYONE

Same contract, governed

Nothing here is exotic. It is the same accrual, done so the number sees the cliff coming, moves smoothly, and can be proven on demand.

Forecast, don't assume	Accrue against a live re-forecast of full-period volume, refreshed from actual run-rate — not last year's landing spot. The moment run-rate points past \$12M, the model knows.
Model the tier as a step	Represent the retroactive tier as a probability-weighted step function . As the odds of crossing \$12M rise, the reserve rises with them — the catch-up is built up over months, not discovered in December.
Re-estimate every period	Treat each close as a change in estimate (ASC 705-20): adjust prospectively as expectations move. The swing is absorbed in small increments, never one lump.
Make it reconstructable	Every accrual ties to its inputs — contract, qualifying volume, rate, the estimate basis — with who approved it and when. Ask "how did we get this number in August?" and the answer is a click, not a three-day dig.

Under the governed version, the Q4 "surprise" is a **\$12K** final adjustment, not a **\$160K** one — because the other \$148K was already reserved, smoothly, as the customer climbed. Same money owed. No blindside.

SECTION 04 — THE PRINCIPLE

The number you accrue is a guess — until it's reconstructable.

Every failure in this teardown is the same failure wearing four hats: an accrual the team couldn't *see moving* and couldn't *prove after the fact*. Fix those two and your \$X stops being a surprise — it becomes a number you see coming and can prove on demand.

That is the whole of what governed accrual means: the number forecasts itself forward, moves in small honest steps, and traces back to its source on demand. Argus is built to do exactly that — but the discipline above is worth adopting whether the tool is ours or a better spreadsheet.