

Board Decides to Defer Implementation of Cost Accounting Standards

As reported in the August **FASAB News** (Issue 45, pp 1-2), the Board considered a request by the Chief Financial Officers Council for a two year deferral of the effective date of the standards prescribed in SFFAS 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*, from fiscal year 1997 to fiscal year 1999. After careful consideration, the Board reluctantly agreed to propose a one year deferral to fiscal year 1998, and issued an exposure draft for that proposal. (The entire exposure draft was published as an attachment to the August 1997 issue of **FASAB News**.) The original effective date of SFFAS 4 was for periods beginning after September 30, 1996. The proposed effective date is for periods beginning after September 30, 1997. The Chief Financial Officers Council had also requested that certain parts of SFFAS 7, *Accounting for Revenue and Other Financing Sources*, that dealt with cost, be deferred for one year from their current implementation date of fiscal year 1998, to fiscal year 1999. The Board, however, did not agree with that request.

A total of 26 responses to the exposure draft were received. At the September 26, 1997 Board meeting, Board members reviewed comments provided by the respondents to the exposure draft, and discussed the following issues:

- Should the proposed one year deferral of the effective date to periods beginning after September 30, 1997, be finalized?

- In addition to deferring the effective date, should agencies be given a transition period within which

On Interpretation 2: Interpretation 2, *Accounting for Treasury Judgment Fund Transactions*, was issued in January 1997. It requires that if a loss in litigation is probable and estimable, the reporting entity in the litigation should recognize an expense and liability for the full amount of the estimated loss, although the loss may be paid by the Treasury Judgment Fund. Since the Interpretation is predicated in part on the full cost principle in SFFAS 4, the exposure draft to defer the

they can reach full compliance with SFFAS 4 requirements?

- If SFFAS 4 is deferred, should Interpretation 2, *Accounting for Treasury Judgment Fund Transactions*, be deferred?

- Should the request to delay certain parts of SFFAS 7 be reconsidered?

- Should the final statement include suggestions to FASAB principals (the Secretary of the Treasury, the Director of the Office of Management and Budget, and the Comptroller General) that were provided by respondents to the exposure draft?

The Board's Decisions

On SFFAS 4: The Board agreed, "with reluctance," to recommend to the FASAB principals a one year deferral of the effective date of the cost accounting standards to fiscal year 1998. Further, the Board agreed that the implementation date should be definitive and that a transitional period to reach full compliance after the effective date should not be provided. It believes that such a transitional period would add uncertainty to the implementation date, and pointed out that flexibility in developing costing methodologies is already built into the standards. Moreover, the Board believes that without timely implementation of the cost accounting standards, the success in reporting outputs, outcomes and associated costs for the Government Performance and Results Act will be jeopardized. Finally, the Board generally agreed that there should be no additional leeway after the one year delay.

effective date of SFFAS 4 asked the question, "If SFFAS 4 were deferred as proposed, should Interpretation 2 be deferred as well?" After considering the responses, the Board agreed not to defer Interpretation 2; the underlying principle of Interpretation 2 is the recognition of contingent liabilities required in SFFAS 5, *Accounting for Liabilities*, which was effective for fiscal year 1997.

On SFFAS 7: Some respondents restated the Chief Financial Officers Council's request that some cost-related portions of SFFAS 7 be deferred to fiscal year 1999. Although the Board decided to make the cost accounting standards effective for fiscal year 1998, it reiterated its position not to defer any part of SFFAS 7, which already is effective for fiscal year 1998. The Board believes that it is important to link together SFFAS 4 and 7, because provisions in SFFAS 7 bring cost information into focus in measuring operating results.

On Forwarding Suggestions to FASAB Principals: Many respondents suggested approaches that may encourage implementation of the cost accounting standards. The Board agreed that some of the suggestions should be conveyed to the FASAB principals. Those suggestions will be forwarded in the Chairman's letter transmitting the Statement of Recommended Accounting Standards to defer the effective date of SFFAS 4.

FASAB staff has submitted a draft Statement of Recommended Accounting Standards as discussed above to Board members for review. After Board concurrence, the draft Statement of Recommended Accounting Standards will be forwarded to the FASAB principals for approval.

For further information, contact Richard Mayo, 202-512-7356, or email mayor.fasab@gao.gov.

Coast Guard Addresses Board

For several months, the Board has been working to create a definition of "national defense property, plant, and equipment" (to replace "federal mission property, plant, and equipment"). For background, see **FASAB News**, issues 40-41, and 43-46. In conjunction with this issue, the representatives from the Coast Guard had addressed the Board in January 1997, proposing to the Board that Coast Guard aircraft and cutters (vessels over 65 feet) be considered national defense property, plant, and equipment (PP&E). However, after considerable discussion, the Board had tentatively decided that national defense PP&E would include only weapons systems used by military departments, and the Maritime Administration's Naval Defense Reserve

Fleet ships. It also tentatively decided that Coast Guard aircraft and cutters should be capitalized and depreciated, with depreciation being allocated based on functions.

In response to the Coast Guard's request for an additional audience with the Board, representatives of the Coast Guard were invited to comment on the Board's tentative decisions. At its September meeting, Messrs. William Campbell, and Michael Reed, and Rear Admiral T.W. Allen expressed frustration at being unable to communicate what they believed were unique aspects of Coast Guard cutters and aircraft. They also stated that:

- The Coast Guard is considered a part of the "armed forces" and is the only entity outside the Department of Defense that has this distinction.
- The Coast Guard annually is included in the national military strategy developed by the Department of Defense, and it participates in joint training exercises with other armed forces.
- They believe that the intended use of these assets (for defense purposes), not their predominant use (for other than defense purposes), should be considered in classifying the assets.
- The Coast Guard currently has the capability to depreciate its cutters and aircraft and is doing so for internal management and reimbursement purposes.

Chairman Mosso reminded the Board members that the issues had already been decided and that further debate was not warranted. However, he asked if Board members had questions of a clarifying nature. A Board member noted that, since the Coast Guard indicated that it has the capability to depreciate its cutters and aircraft, he assumed that its primary concern with having its aircraft and cutters categorized as general PP&E was that unfavorable cost comparisons could be made of those assets with similar but non-defense-type assets. The Coast Guard confirmed this concern. They also said they believed that such comparisons could bias the choice of PP&E to be acquired by the Coast Guard, which could have a negative effect on military preparedness.

There were no further questions and the Chairman thanked the Coast Guard representatives.

For further information, contact Rick Wascak, 202-512-7363, or email wascakr.fasab@gao.gov.

Department of Defense Presents Illustrative Report on National Defense PP&E

Continuing the discussion of the Board's actions on modifying the stewardship reporting category of national defense PP&E (see above related article), the Board recently has been focusing its efforts on the specific reporting requirements it will propose for that category. As reported in last month's edition of **FASAB News**, the Board decided that the standard should not require use of a specific data source, for example the Selected Acquisition Report prepared by the Department of Defense. Instead, entity management should have the discretion of choosing the best data sources to meet reporting requirements. With that in mind, at the August Board meeting, the Department of Defense Board member, Mr. Nelson Toye, volunteered to prepare an illustrative report of the type of information the Department of Defense would expect to report as national defense PP&E.

At the September Board meeting, Mr. Toye and the Department's Director of Accounting Policy, Mr. De Ritchie, presented the Department of Defense's suggestion for an illustrative stewardship report. Mr. Toye suggested that such an illustrative report could convey the reporting requirements of the standard in lieu of the text of the standard providing specific reporting requirements and data sources.

The illustrative report was developed jointly with the military departments--the Departments of the Army, Air Force, and Navy. The objectives in developing the report were to present unclassified information in a format that is concise, readable, and understandable. In the report, for each category of National Defense PP&E, each military department is represented by one page of funding trend information and another page of quantity information. Although information on the condition of the PP&E and deferred maintenance was not included, Mr. Toye stated that the Department of

Defense expects to report this information once it has resolved difficulties in the information gathering.

Although Messrs. Toye and Ritchie acknowledged that more work needs to be done on the illustrative report, Chairman Mosso said that the reporting classifications were sound and that the illustrative report would provide a good sample report to include in the soon-to-be-issued technical amendment exposure draft to Statements of Federal Financial Accounting Standards 6, *Accounting for Property, Plant, and Equipment*, and 8, *Supplementary Stewardship Reporting*. He indicated that continued work by the Department of Defense and comments on the exposure draft could be used to finalize the illustrative report that would appear in the final recommended standards.

For further information, contact Rick Wascak, 202-512-7363, or email wascakr.fasab@gao.gov.

Board Begins to Finalize Its Approach to Social Insurance

For some time, the Board has been discussing how and what should be reported in Federal financial statements for social insurance programs (see recent coverage in **FASAB News**, issues 42, 43, and 45). After analyzing the primary social insurance programs of Old Age Survivors and Disability Insurance, otherwise known as Social Security, and Medicare, the Board decided to recognize liabilities for such programs when payments are "due and payable," and to require certain supplementary stewardship information.

At its September meeting, the Board discussed (1) whether to establish definitive criteria for social insurance programs or list the specific programs included in the standard, and (2) which programs, in addition to Social Security and Medicare, should be covered by the standard.

Social Insurance Criteria - The Board discussed whether the standard should provide definitive criteria, or list the specific programs covered and describe typical characteristics. The Board generally acknowledged that its long search had demonstrated that definitive criteria for social insurance -- however desirable -- were elusive. The Board agreed that the standard should describe "characteristics" rather than try to set definitive "criteria."

The Board agreed on six characteristics for social insurance programs:

1. Sponsorship and regulation by the Federal Government.
2. Financing from, or on behalf of, participants.
3. Eligibility derived from taxes and/or fees paid.
4. Benefits not directly related to taxes and/or fees paid.
5. Benefits prescribed in law.
6. Intended for the general public and not solely for federal employees.

Moreover, the Board will list in the standard the specific programs covered, and will provide for any further additions of programs to the list; decisions on inclusion will not be at the discretion of the agencies.

Additional programs - A second issue was: which programs, in addition to Social Security and Medicare, should be included in the social insurance standard. Prior to discussing other potential programs, the Board heard from Mr. Ken Bresnahan, acting Chief Financial Officer of the Department of Labor. Mr. Bresnahan advocated including two programs under the Department's purview, the Black Lung Benefits and the Unemployment Insurance programs. Mr. Bresnahan said that he believed that the Black Lung Benefits and Unemployment Insurance programs meet the social insurance criteria and should be accounted for in a manner similar to Social Security and Medicare.

After discussing various programs, the Board agreed to include Railroad Retirement, and Black Lung Benefits in the social insurance standard. The Board also tentatively agreed to include Unemployment Insurance, but directed the staff to develop alternative supplementary stewardship information on Unemployment Insurance for the Board's review before making a final decision. Other programs, such as veterans benefits and the Pension Benefit Guarantee Corporation were not included since it was agreed that SFFAS 5, *Accounting for Liabilities of the Federal Government*, covered these and other programs and was satisfactory at this time.

Reporting improper payments - A third issue involved reporting improper payments. During its first comprehensive audit of Medicare records, the Inspector General of the Health and Human Services Department

sampled 5,300 claims; it found problems with 14 percent of the payments (or \$23 billion). The problems ranged from lack of documentation (47 percent) and improper coding, to fraud.

As the Board discussed if, or how, to report improper payment information, discussion turned to whether a detailed reporting standard should be developed, either as part of the social insurance project, or as a separate project. The Board decided that the scope of the issue was much larger than Medicare. For example, improper payments could be material for grants, general assistance (Food Stamps, Aid to Families with Dependent Children, etc.), and other programs. Therefore, if the Board were to address reporting improper payments, it should be done outside of the social insurance standards.

The Board generally agreed that reporting of improper payments would provide performance and management information. Moreover, such information could improve control over payments throughout an agency and assist the auditor. Board members noted that when payments are reported on a financial statement, management is asserting that the payments are valid. If the propriety of payments were in question, at the least, footnote disclosure providing qualitative information about the validity of the payments might be desirable. The Board agreed that the scope of such a project would be complex, but that the issues should be researched.

The Board anticipates issuing an exposure draft on social insurance standards by the end of the calendar year.

For further information, contact Richard Fontenrose, 202-512-7358, or email fontenrosr.fasab@gao.gov.

National Science Foundation Request for Guidance (continued)

At the August Board meeting, representatives of the National Science Foundation requested guidance from the Board on deciding whether to apply SFFAS 6, *Accounting for Property, Plant, and Equipment*, or SFFAS 8, *Supplementary Stewardship Reporting*, to property, plant, and equipment (PP&E) acquired and/or

used by grant awardees for which the National Science Foundation holds title, but for which it is prohibited by law from controlling or operating (see *FASAB News*, issue 46).

At its September meeting, the Board continued its August discussion. The National Science Foundation's Chief Financial Officer, Mr. Joseph L. Kull, and Deputy Chief Financial Officer, Mr. Al Muhlbauer, were available to answer the Board's questions.

The Board's discussion centered on whether the accounting and reporting entity for the PP&E should be based on 1) who controls the asset; 2) who picks up the operating costs of the asset; 3) who gets the economic benefit from the asset; or 4) who holds title to the asset.

Some Board members suggested that the question was one addressing reporting entity issues, and that Statement of Federal Financial Accounting Concepts 2, *Entity and Display*, should be researched. Other members focused on the language of the standards in SFFAS 6, specifically paragraphs 17 - 19. The paragraphs define what PP&E consists of and what it "also includes." Board members disagreed on whether the language in the standard would include or exclude the PP&E in question. Members generally agreed that, although some guidance to the National Science Foundation was in order, a special interpretation should not be issued at this time. Instead, the language of the PP&E standard should be further examined and may need clarification.

Chairman Mosso asked the staff to further research the issues and present possible approaches for resolving the question posed by the National Science Foundation. The Board will continue its discussion of this area at its October 24 meeting.

For further information, contact Wendy Comes, 202-512-7357, or email comesw.fasab@gao.gov.

Highlights of September AAPC Meeting

The most recent meeting of the Accounting and Auditing Policy Committee (AAPC) was held on September 12. Discussion focused on three issues:

(1) Who has responsibility for providing legal representation letters?

The Committee reviewed draft guidance for agencies on legal representation letters. Primary concerns were that current systems (databases) for tracking litigation handled by the Department of Justice are not adequate. In addition, internal controls at each agency may not result in reliable and complete case listings. Representatives from the Department of Justice were present to give their views on who should take the lead in providing legal representation letters. The Committee generally agreed that each agency's General Counsel should take the lead. Committee member Bill Pugh of the Department of the Treasury will present a revised issue paper at the October meeting.

(2) What determines whether environmental liabilities are probable and estimable?

The Committee reviewed and gave tentative approval of guidance on environmental liabilities. Minor edits were discussed. It was agreed that, after editing, the document would be circulated to AAPC members for a fatal flaw review, to FASAB for approval, and then to the Office of Management and Budget.

(3) What schedules should be established for preparation and audit of interagency confirmations of audit assurance?

Committee member Bob Dacey of the General Accounting Office reported on progress in working with the Office of Personnel Management and the Social Security Administration. Procedures for audit assurance should be obtained on pension expense. Agency consensus should be obtained. The AAPC will leave this item on the agenda as a long-range issue and obtain interim reports on progress.

Agenda Committee Recommendations

The Agenda Committee presented the following issues for consideration by the AAPC:

- When documentation to support the cost of general PP&E is not available, what acceptable alternatives are available to arrive at a value for financial reporting purposes?

- Should the footnotes to the Department of Labor's statements disclose, for the Black Lung Disability Trust Fund, the present value of estimated future benefit payments for existing claims?
- Should costs incurred by the Drug Enforcement Administration to alter or modify space prior to the Drug Enforcement Agency occupying the space be accounted for as leasehold improvements or as expense in the period incurred?

AAPC members agreed to add the first issue to their agenda for future consideration; the second and third issues were not added.

October Meeting

The next meeting of the AAPC will be held October 9 in Room 4N30 of the GAO Building, 441 G St., N.W., Washington, DC 20548.

For further information, contact Dick Tingley at 202-512-7361, or email at tingleyr.fasab@gao.gov.

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Upcoming Meeting Agendas

October 24 FASAB Meeting: 1) Consider the accounting for certain PP&E acquired with grant funds; 2) review of draft statement on Management's Discussion and Analysis; 3) discuss issues on social insurance programs; and 4) review a draft exposure draft amending SFFAS 6, *Accounting for Property, Plant, and Equipment*.

November 7 FASAB Meeting: 1) Hold a public hearing on Internal Use Software; 2) review a draft Statement of Recommended Accounting Standards on Governmentwide Supplementary Stewardship; and 3) consider additional issues on social insurance.

October 9 AAPC Meeting: 1) Review draft guidance on legal representation letters and progress report on resolving the completeness/internal control issues; 2)

review draft guidance on environmental liabilities; 3) review status report on inter-agency and intra-agency confirmations; 4) review status report on estimation on undocumented property, plant, and equipment; 5) review agenda committee recommendations on issues to decide; and 6) assign issues added to the agenda to members.

NOTE:

Since the October and November FASAB Meetings are so close, coverage of the October meeting will be provided after the November meeting in an expanded issue of the *FASAB News*.

FASAB's Home Page:
<http://www.financenet.gov/fasab.htm>

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