

**Exposure Draft- Questions for Respondents due February 4, 2016**

*Establishing Opening Balances for General Property, Plant, and Equipment: Amending Statement of Federal Financial Accounting Standards (SFFAS) 6, SFFAS 10, SFFAS 23, and Rescinding SFFAS 35*

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Organization: Department of the Army

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Q1. The Board proposes a reporting entity be permitted to apply an alternative valuation method in establishing opening balances for general property, plant, and equipment (PP&E) when presenting financial statements, or one or more line items addressed by this Statement, following generally accepted accounting principles (GAAP) promulgated by the Federal Accounting Standards Advisory Board (FASAB) either (1) for the first time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method.

The proposed Statement describes the alternative valuation method and related disclosures.

**a) Do you agree or disagree with the proposal to permit opening balances of general PP&E to be valued based on deemed cost? Please provide your rationale.**

The Army agrees with the proposal to permit opening balances based on deemed cost. The flexibility afforded by the deemed cost approach achieves an appropriate balance between the value of the information presented in the financial statements and the cost to capture and report that information. Statement of Federal Financial Accounting Concept 1 Chapter 5 directs the standards setters to consider the relative benefit and cost of financial reporting information when developing standards. Adding the deemed cost approach to the standards better balances the benefit and cost of the information presented.

The concept of balancing the value of information and the cost to report that information also supports Army disagreement with parts of this Exposure Draft. As discussed further in the responses to Q4, the Army does not agree with any effort to restrict the ability to use estimates of historical cost for balances after opening balances have been established. Current standards explicitly support methodologies for the estimation of historical cost based on "amounts to be expended". SFFAS 35 does not require transaction based data but rather "**encourages** those federal entities that use estimates to approximate the historical cost values of G-PP&E to establish processes and practices (i.e., adequate systems and internal control practices) for future acquisitions that will capture and sustain transaction based data."

The Army is working towards transaction level support for historical costs across all components of PP&E. Achieving that goal is several years in the future and will not be achieved at a single point in time for all components of PP&E. Therefore, an unreserved assertion of the value of all PP&E and a simultaneous shift to transaction based support for historical cost across all components of PP&E is simply not possible in the next several years.

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**b) Do you agree or disagree that the related disclosures are appropriate?  
Please provide your rationale.**

The Army agrees that the methods to value opening balance should be disclosed as the information will be valuable to the reader's understanding of the values presented. The Army disagrees with the statement that "subsequent periods need not repeat this disclosure". This statement should be changed to say that the disclosures should be included in all periods where alternate valuation methods are used as Army and many reporting entities will be using alternate methods in subsequent reporting periods in accordance with current standards.

Q2. The Board proposes to amend Statement of Federal Financial Accounting Standards (SFFAS) 6, *Accounting for Property, Plant, and Equipment*, so that land categorized as general PP&E may be excluded from the opening balances of general PP&E. Instead, disclosures would reveal the acres of land and changes in those acres over time. A reporting entity electing to exclude land from its general PP&E opening balance should continue to exclude future land acquisition amounts and provide the disclosures.

Some members suggested valuing existing land holdings based on a set amount per acre of land or deemed cost. For example, one study estimated the land value in the United States at roughly \$4.5 trillion in the third quarter of 2009. Since the number of acres in the United States is almost 2.3 billion, this equates to approximately \$2,000 per acre. (Land values vary greatly based on location, potential use, and availability and cost of financing.) These members are interested in receiving comments on the usefulness of a general valuation approach that could be applied government-wide.

The Board intends to begin a project on land in the near future that would review existing standards and consider a consistent approach. Based on the results of that project, the decisions made for opening balances and future acquisitions of land in this Statement may be revised. Also, some members suggested deferring any changes in the historical basis for land acquired for use in operations until the Board completes a re-examination of the appropriate basis of accounting for land.

(See par. 12.d. and 12.g. for relevant standards and par. **Error! Reference source not found.- Error! Reference source not found.** for a discussion of certain members' concerns and **Error! Reference source not found.** in the Basis for Conclusions.)

**a) Do you agree or disagree with the proposal to allow exclusion of land from the opening balances of general PP&E even though other component reporting entities will report the cost of certain land in general PP&E?**

The Army agrees with the proposal to exclude land from PP&E balances. Army land has been acquired over more than two centuries. Reporting land at its cost, either estimated or based on transaction detail, does not appear to provide much benefit to readers of the financial statements relative to the cost to develop and maintain the values.

**If you disagree, do you prefer (1) to value land holdings based on existing standards requiring historical cost of land acquired in connection with**

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**other general PP&E to be capitalized, a set amount per acre of land, deemed cost, or another valuation method, (2) to defer any changes in the current requirements until the Board completes a reexamination of the appropriate basis of accounting for land, or (3) to adopt another option? Please provide your rationale.**

- b) Do you agree or disagree that the related disclosures are appropriate? Please provide your rationale.**

The Army agrees.

- c) Do you agree or disagree that a reporting entity electing to exclude land from its general PP&E opening balances should continue to exclude future land acquisition amounts? Please provide your rationale.**

The Army agrees.

- d) The Board anticipates a project on land to review existing standards and to consider a consistent approach for all component reporting entities. Please provide any suggestions you have for improving current reporting on land.**

If standards require land to be reported in financial statements, consider whether it should only be reported on the financial statements of the United States and not on the statements of each reporting entity. Federal land is in the possession of individual Departments but the Federal government from time to time shifts the possession between Departments creating a potential justification that the land is under the control of the United States and not it's individual Departments.

- Q3. The Board proposes to amend SFFAS 10, *Accounting for Internal Use Software*, to allow a reporting entity to choose among alternatives in establishing an opening balance for internal use software when presenting financial statements, or one or more line items addressed by this Statement, following generally accepted accounting principles (GAAP) promulgated by the Federal Accounting Standards Advisory Board (FASAB) either (1) for the first time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method. The Statement provides for selecting between (1) an alternative valuation method of deemed cost that is consistent with that provided for all general PP&E and (2) prospective capitalization of internal use software.

The proposed Statement describes the alternatives and related disclosures. (See par. **Error! Reference source not found.-Error! Reference source not found.** for relevant standards and par. **Error! Reference source not found.- Error! Reference source not found.** and **Error! Reference source not found.** in the Basis for Conclusions.)

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- a) **Do you agree or disagree with the proposal to allow a reporting entity to choose among alternatives in establishing an opening balance for internal use software? Please provide your rationale.**

The Army partially agrees with the proposal. Prospective capitalization of Internal Use Software as the only option and removal of alternate valuation methods will enhance consistency while also appropriately balancing the value of the information in the financial statements with the cost of reporting that information.

- b) **Do you agree or disagree that the related disclosures are appropriate? Please provide your rationale.**

To align with the Army position above, the disclosure of alternate valuation methods are not needed.

- Q4. The Board proposes to rescind SFFAS 35, *Estimating the Historical Cost of General Property, Plant, and Equipment: Amending Statements of Federal Accounting Standards 6 and 23*, because this Statement would provide comprehensive guidance for establishing opening balances. The Board has incorporated the relevant components of SFFAS 35 in the proposed guidance in this Statement. The Board did not incorporate language from SFFAS 35 that explicitly allows for reasonable estimates on a go-forward basis to identify the cost of newly-acquired or constructed general PP&E. t

Instead, the Board acknowledges that reasonable estimates are permitted in the preparation of financial statements, with or without the existence of SFFAS 35, and are acceptable without guidance from the Board. (See par. **Error! Reference source not found.-Error! Reference source not found.** for relevant standards and par. **Error! Reference source not found.- Error! Reference source not found.** in the Basis for Conclusions.)

- a) **Do you agree or disagree with the proposal to rescind SFFAS 35? Please provide your rationale.**

While the Army agrees that reasonable estimation of values and costs are always acceptable under accounting concepts and standards, the Army disagrees with the proposal to rescind SFFAS 35. SFFAS 35 and the subsequent Technical Release 13 are valuable to reporting entities by providing additional needed clarifications to the standards for use of estimation methods. Without these issuances, reporting entities do not have clarity to develop consistent estimation methodologies across the components of a reporting entity. Further, independent auditors rely on these documents to inform their judgment on the reasonableness estimation methodologies. Specifically, an auditor can safely determine that an estimation approach listed in the standards and technical release is more than likely reasonable.

The original release of SFFAS 6 in 1995 discussed like-items and indexed like-items as the only two applicable reasonable estimate methods. The release of SFFAS 23 in 2003 noted that

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information based on “amounts to be expended” were also ways to achieve a reasonable estimate. When SFFAS 6 and SFFAS 23 were modified and linked together by SFFAS 35 in 2009 the estimation methodologies became more reasonable and acceptable for both accounting and audit purposes.

The change SFFAS 35 made to SFFAS 6, para. 40 reinforces the acceptability of the range of estimation methods:

“Although the measurement basis for valuing G-PP&E remains historical cost, reasonable estimates may be used to establish the historical cost of G-PP&E, in accordance with the asset recognition and measurement provisions herein. Estimates may be based on:

- cost of similar assets at the time of acquisition,
- current cost of similar assets discounted for inflation since the time of acquisition (i.e., deflating current costs to costs at the time of acquisition by general price index), or
- other reasonable methods, including those estimation methods specified in SFFAS 23 paragraph 12.”

The guidance below from SFFAS 23, para. 12 added to SFFAS 6, para. 40, provides the Army and other reporting entities with the ability to use a range of acceptable estimation methods.

“Estimates may be based on information such as, but not limited to, budget, appropriations, engineering documents, contracts, or other reports reflecting amounts to be expended.”

Paragraph 9 of SFFAS 35 clearly indicates that reporting entities can use estimates not only to establish initial balances but also to estimate balances in subsequent periods for those entities that previously established PP&E balances

“Reasonable estimates may be used upon initial capitalization as entities implement G-PP&E accounting for the first time, as well as by those entities who previously implemented G-PP&E accounting.”

**b) Do you agree or disagree that reasonable estimates are permitted in the preparation of financial statements, with or without the existence of SFFAS 35? Please provide your rationale.**

As is discussed above, the Army agrees that reasonable estimation of values and costs are always acceptable under accounting concepts and standards. However, the Army disagrees with the proposal to rescind SFFAS 35 for the reasons stated above.

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**COMMENTS ON RELATED MATTERS:**

The Army plans to use the full range of estimation methods described in the standards. Based on pilot implementation of several of the methods, the Army believes the historical cost values are reasonable and can be supported with the supporting documentation appropriate to the method as described in Technical Release 13. The methods Army plans to employ have been used by other reporting entities that have received unmodified opinions from independent auditors. There are no barriers to implementation of the current GAAP and until an actual issue from an independent auditor arises, the Army believes there is no issue for FASAB to address related to use of estimated cost methods for PP&E valuation. The Army recommends that FASAB maintain the current GAAP related to the estimation of historical cost of PP&E as defined in SFFAS 6, 23, and 35.