Federal Accounting Standards Advisory Board

CLASSIFICATION AND DISAGGREGATION OF COST

Statement of Federal Financial Accounting Standards

Exposure Draft

Written comments are requested by [date 90 days after issuance]

Month day, year

Working Draft – Comments Are Not Requested on This Draft

THE FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD

The Secretary of the Treasury, the Director of the Office of Management and Budget (OMB), and the Comptroller General, established the Federal Accounting Standards Advisory Board (FASAB or "the Board) in October 1990. FASAB is responsible for promulgating accounting standards for the United States Government. These standards are recognized as generally accepted accounting principles (GAAP) for the federal government.

An accounting standard is typically formulated initially as a proposal after considering the financial and budgetary information needs of citizens (including the news media, state and local legislators, analysts from private firms, academe, and elsewhere), Congress, federal executives, Federal program managers, and other users of federal financial information. The proposed standards are published in an Exposure Draft for public comment. In some cases, a discussion memorandum, invitation for comment, or preliminary views document may be published before an exposure draft is published on a specific topic. A public hearing is sometimes held to receive oral comments in addition to written comments. The Board considers comments and decides whether to adopt the proposed standard with or without modification. After review by the three officials who sponsor FASAB, the Board publishes adopted standards in a Statement of Federal Financial Accounting Standards. The Board follows a similar process for Statements of Federal Financial Accounting Concepts, which guide the Board in developing accounting standards and formulating the framework for federal accounting and reporting.

Additional background information is available from the FASAB or its website:

- "Memorandum of Understanding among the Government Accountability Office, the Department of the Treasury, and the Office of Management and Budget, on Federal Government Accounting Standards and a Federal Accounting Standards Advisory Board."
- "Mission Statement: Federal Accounting Standards Advisory Board", exposure drafts, Statements of Federal Financial Accounting Standards and Concepts, FASAB newsletters, and other items of interest are posted on FASAB's website at: www.fasab.gov.

Copyright Information

This is a work of the U. S. government and is not subject to copyright protection in the United States. It may be reproduced and distributed in its entirety without further permission from FASAB. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.

Contact us:

Federal Accounting Standards Advisory Board
441 G Street, NW, Suite 6814
Mail stop 6H19
Washington, DC 20548
Telephone 202-512-7350
FAX – 202-512-7366
www.fasab.gov

Federal Accounting Standards Advisory Board

ISSUE DATE

TO: ALL WHO USE, PREPARE, AND AUDIT FEDERAL FINANCIAL INFORMATION

Your comments on the exposure draft of a proposed Statement of Federal Financial Accounting Standards, entitled Classification and Disaggregation of Cost, are requested. Specific questions for your consideration appear on page 7 but you are welcome to comment on any aspect of this proposal. If you do not agree with the proposed approach, your response would be more helpful to the Board if you explain the reasons for your position and any alternative you propose. Responses are requested by DUE DATE.

All comments received by the FASAB are considered public information. Those comments may be posted to the FASAB's website and will be included in the project's public record.

Mail delivery is delayed by screening procedures. Therefore, please provide your comments in electronic form by e-mail to fasab@fasab.gov. If you are unable to e-mail your responses, we encourage you to fax the comments to (202) 512-7366. Alternatively, you may mail your comments to:

Wendy M. Payne, Executive Director
Federal Accounting Standards Advisory Board
Mailstop H19
441 G Street, NW, Suite 6814
Washington, DC 20548

We will confirm receipt of your comments. If you do not receive confirmation, please contact our office at 202.512.7350 to determine if your comments were received.

The Board's rules of procedure provide that it may hold one or more public hearings on any exposure draft. No hearing has yet been scheduled for this exposure draft. or A public hearing has been scheduled at 9:00 AM on Month Day, Year, in Room 7C13 at the GAO Building, 441 G Street, NW, Washington, D.C.

Notice of the date and location of any public hearing on this document will be published in the Federal Register and in the FASAB's newsletter.

Sincerely,

Tom L. Allen

Chairman

EXECUTIVE SUMMARY

WHAT IS THE BOARD PROPOSING?

The Board is proposing standards for how federal component reporting entities classify and disaggregate costs in the statement of net cost. The Board is also proposing standards for related disclosures about the basis for the classification approach used in reporting costs and any changes from the previous reporting period.

HOW WOULD THIS PROPOSAL IMPROVE FEDERAL FINANCIAL REPORTING AND CONTRIBUTE TO MEETING THE FEDERAL FINANCIAL REPORTING OBJECTIVES?

Federal reporting entities can be complex organizations that provide a diversity of services to the public and they often seek to reasonably meet the information needs of a variety of stakeholders. Those stakeholders could range from program advocacy groups to Congressional oversight committees. While all the stakeholders may seek information about the entity's total costs, individual groups expect to examine the details from different perspectives. For example, some may expect to examine costs classified by strategic goal, while others may expect to examine costs classified by budget function or individual program.

Also, some cost items respond differently to different economic events. For example, costs associated with general management and administrative support may not be directly affected by a change in the number of eligible grant recipients. Additionally, other costs may be incurred during the current reporting period but are intended to increase economic growth or provide benefits to the nation over a long period. Accordingly, adequately disaggregating line items on the statement of net cost can provide useful information regarding the nature of the costs that the entity incurred. Because it is not practical to present each possible classification and level of disaggregation, this proposal provides guidance to help federal entities consistently determine the classification approach and the level of disaggregation that should be used when reporting on costs.

In addition, analysts and other users often intend to compare costs among reporting entities and compare an entity's costs over time to identify trends. However, each individual entity may select a different approach for classifying and disaggregating its costs and comparisons among entities may not always be feasible. Also, as a result of various factors, such as a new legislative requirement, an entity could change its classification and disaggregation structure from one reporting period to the next. Consequently, this proposal requires entities to disclose information to assist users in understanding why the entity selected a particular structure and any changes in the structure from the previous reporting period.

TABLE OF CONTENTS

Executive Summary 1
What is the Board proposing? 1
How would this proposal improve federal financial reporting and contribute to meeting the federal financial reporting objectives? 1
Table of Contents 2
Questions for Respondents 3
Introduction 4
Purpose 4
Materiality 5
Proposed Standards 6
Scope 6
Definitions 6
Recognition and Measurement 6
Disclosure Requirements 7
Component Reporting Entity Disclosures 8
Financial Report of the US Government Disclosures ..... **Error! Bookmark not defined.**
Effective Date 8
Appendix A: Basis for Conclusions 9
Project history 9
Appendix B: Illustrations 10
Appendix C: Abbreviations 11
Appendix D: Glossary 12

QUESTIONS FOR RESPONDENTS

The Board encourages you to become familiar with all proposals in the Statement before responding to the questions in this section. In addition to the questions below, the Board also would welcome your comments on other aspects of the proposed Statement. Because the proposals may be modified before a final Statement is issued, it is important that you comment on proposals that you favor as well as any that you do not favor. Comments that include the reasons for your views will be especially appreciated.

The Board believes that this proposal would improve federal financial reporting and contribute to meeting the Federal financial reporting objectives. The Board has considered the perceived costs associated with this proposal. In responding, please consider the expected benefits and perceived costs and communicate any concerns that you may have in regard to implementing this proposal.

The questions in this section are available in a Word file for your use at www.fasab.gov/exposure.html. Your responses should be sent by e-mail to fasab@fasab.gov. If you are unable to respond by e-mail, please fax your responses to (202) 512-7366. Alternatively, you may mail your responses to:

Wendy M. Payne, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6H19
441 G Street, NW, Suite 6814
Washington, DC 20548

All responses are requested by [insert date].

Q1. Paragraph XX of the proposed Statement discusses principles for classifying and disaggregating costs in financial statements.
   a. Do you agree or disagree with the principles for classifying costs?
   b. Do you agree or disagree with the principles for disaggregating costs?

Q2. Paragraph XX of the proposed Statement discusses criteria for classifying costs on the face of the statement of net cost. Do you agree or disagree with the criteria?

Q3. Paragraph XX of the proposed Statement discusses criteria for disaggregating costs. Do you agree or disagree with the criteria?

Q4. Paragraph XX of the proposed Statement discusses disclosure requirements to assist users in understanding the basis for the classification and disaggregation approach used. Do you agree or disagree with the requirement?

INTRODUCTION

PURPOSE

1. Statement of Federal Financial Accounting Concepts (SFFAC) 1, Objectives of Federal Financial Reporting, discusses the information that users expect to review in financial reports and what information should be provided. The conceptual guidance explains that financial reporting should provide information to help readers determine "the costs of providing specific programs and activities and the composition of, and changes in, these costs."

2. SFFAC 2, Entity and Display, provides different displays to help achieve the reporting objectives and explains that total and net cost of services is the most useful information that a flow statement could provide. Accordingly, a statement of net cost would assist readers in determining the cost of providing programs and activities and the composition of and changes in these costs.

3. SFFAC 2 also provides a variety of approaches that could be used in classifying costs in the statement of net cost. The guidance discusses that costs could be classified by sub-organization, program, or object class or a combination of these. However, the guidance notes that the definition of the term program "varies in the eye of the beholder." Also, some reporting entities have determined other approaches are needed to help link costs to performance information. They may classify costs by strategic goal or strategic objective.

4. Also, some entities with several programmatic activities may decide to aggregate costs into a few broad categories or line item descriptions in the statement of net cost. This approach could result in highly aggregated data that removes the detail necessary to analyze the operations of the entity and the nature of the costs. For example, if an entity reports significant liabilities for loan guarantees on the balance sheet and only reports the total cost of each strategic goal, users will not be able to discern the costs associated with the guarantees when reviewing the statement of net cost.

5. The Board recognizes that, given their unique characteristics and constituencies, each reporting entity could classify and disaggregate costs differently and that prescribing one structure would not be appropriate for all entities. Also, it is not feasible for entities to report cost using all the possible classification and disaggregation approaches and management may determine the need to change from an approach used in previous reporting periods.

6. The objective of the proposed Statement is to provide guidance for selecting an approach for classifying costs on the face of the statement of net cost and disaggregating respective line items.

7. Also, this proposed Statement provides guidance for disclosures to assist users in understanding the classification and disaggregation approach used and, if the entity changes its approach from one period to the next, the proposed Statement provides guidance for disclosing the reason for the change.

MATERIALITY

8. The provisions of this Statement need not be applied to immaterial items. The determination of whether an item is material depends on the degree to which omitting or misstating information about the item makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or the misstatement.

PROPOSED STANDARDS

SCOPE

9. This Statement applies to component federal entities that present general purpose federal financial reports in conformance with generally accepted accounting principles as defined by paragraphs 5 through 8 of SFFAS 34, The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board.

10. This Statement does not apply to the government-wide financial report.

11. This Statement does not apply to internal or special purpose reports. Entity management can decide whether this guidance is appropriate and should be used for such reporting.

DEFINITIONS

12. New Terms

RECOGNITION AND MEASUREMENT

BASIC PRINCIPLES

This section could provide principles that state the objectives of the statement of net cost and guide preparers and others in understanding the manner in which the information should be classified and disaggregated in the statement. For example, the section could state:

1. Classifying costs on the face of the statement of net cost should provide information to assist users in understanding the primary activities of the reporting entity.

2. Disaggregating line items on the face of the statement of net cost should assist users in analyzing the composition of the entity's costs and relating these costs to the primary activities of the reporting entity.

In developing the principles, the project would consider user expectations for cost information.

13. Placeholder

Classification Criteria

Considering the Basic Principles determined previously, this section could provide criteria to assist departments and agencies in classifying costs in the statement of net cost. The project would consider user expectations, reporting entity practices, and FASAB guidance and propose an approach that is consistent with the Basic Principles. For example, existing guidance in SFFAS 4 discusses responsibility segments. The responsibility segment approach facilities management discretion and is intended to reflect the major components of the entity.

14. Placeholder for classification (aggregation) criteria

Disaggregation Criteria

Upon determining the approach for line item classifications, this section would consider the Basic Principles and discuss how line items should be disaggregated. The project could consider user expectations, reporting entity practices, and existing guidance and propose an approach that is consistent with the Basic Principles. For example, as part of their primary activities, entities that

- provide transfer payments should report separately the gross cost of the transfer payment and the gross cost of the administering the program
- provide services at a price should separately report the gross cost of the services, earned revenue, and the net cost
- guarantee loans should report separately the costs related to the guarantees

15. Place holder for disaggregation criteria

DISCLOSURE REQUIREMENTS

COMPONENT REPORTING ENTITY DISCLOSURES

This section could discuss requirements for related disclosures. For example, the requirements could state:

To help users understand the operating performance of the entity, regardless of the approach for disaggregating costs, information should be disclosed about:

a. The services the entity provides

b. The activities or lines of work performed

c. The approach used in disaggregating costs

d. Changes in the disaggregation approach

16. Placeholder

EFFECTIVE DATE

17. The requirements of this Statement are effective for reporting periods beginning after September 30, 20XX.

The provisions of this Statement need not be applied to immaterial items.

APPENDIX A: BASIS FOR CONCLUSIONS

This appendix discusses some factors considered significant by Board members in reaching the conclusions in this Statement. It includes the reasons for accepting certain approaches and rejecting others. Individual members gave greater weight to some factors than to others. The standards enunciated in this Statement–not the material in this appendix–should govern the accounting for specific transactions, events, or conditions.

PROJECT HISTORY

A1.

A2.

APPENDIX B: ILLUSTRATIONS

This appendix illustrates the application of the provisions of this Statement to assist in clarifying their meaning. The facts assumed in these examples are illustrative only and are not intended to modify or limit the requirements of this Statement or to indicate the Board's endorsement of the situations or methods illustrated. Additionally, these illustrations are not intended to provide guidance on determining the application of materiality. Application of the provisions of this Statement may require assessing facts and circumstances other than those illustrated here and require reference to other applicable Standards.

APPENDIX C: ABBREVIATIONS

CFR	Consolidated financial report of the U.S. government
ED	Exposure draft
FASAB	Federal Accounting Standards Advisory Board
FASB	Financial Accounting Standards Board
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GASB	Governmental Accounting Standards Board
IPSASB	International Public Sector Accounting Standards Board
OMB	Office of Management and Budget
SFAS	Statement of Financial Accounting Standards (FASB)
SFFAC	Statement of Federal Financial Accounting Concepts
SFFAS	Statement of Federal Financial Accounting Standards

APPENDIX D: GLOSSARY