

**FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD**  
**August 24-25, 2011**  
**Room 7C13**  
**441 G Street NW**  
**Washington, DC 20548**

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***Wednesday, August 24, 2011***

**Administrative Matters**

- **Attendance**

The following members were present throughout the meeting: Chairman Allen, Messrs. Dacey, Granof, Jackson, Reger, Schumacher, Showalter, and Steinberg. Ms. Kearney attended for Ms. Bond. The executive director, Ms. Payne, and general counsel, Ms. Hamilton, were present throughout the meeting.

- **Approval of Minutes**

The minutes of the June meeting were approved electronically before the meeting.

## **Agenda Topics**

- **Survey Responses and Draft Annual Report**

Ms. Payne thanked the members for completing their surveys and for feedback on the results. She indicated that the goal for the meeting was to look at the concerns and suggestions raised and identify any consensus action items.

The first item relates to five-year planning. Ms. Payne indicated that comments from members included some expression of concern regarding the planning process.

Mr. Allen noted that one of the potential projects he supported – electronic reporting – was not supported by a majority of members and he wondered if there is a way to weight the strength of member views.

Mr. Jackson noted that he did not rate that highly because the means of reporting was not within the Board's domain. Others - such as OMB, Treasury or Congress – can influence the way information is reported. He agreed electronic reporting is very important.

Ms. Payne explained that the Association of Government Accountants (AGA) is undertaking a research project on electronic reporting. She has also been in touch with GASB about electronic reporting and their efforts in that area. Further, she noted that the five-year plan would be revisited periodically during the five-years to consider emerging issues or other new developments.

Mr. Showalter agreed with Mr. Jackson. He also supported keeping the lines of communication open since how you report may lead to changes in the reporting model.

Mr. Steinberg stated that he believes electronic reporting will affect the Board. He noted issues such as the boundaries of information prepared in accordance with generally accepted accounting principles and timeliness. He asked for more details about the AGA study.

Ms. Payne indicated that a small sum had been made available and that AGA may leverage that amount by using a task force. Mr. Steinberg noted AGA research reports are good but are not the same as setting standards. He asked if we could have the AGA task force also work for FASAB. Ms. Payne indicated that she had asked for input from AGA about the role of standards-setters and any pressing standards issues in an electronic reporting environment. She noted that we could always invite the AGA task force to transition to a FASAB task force after the AGA research report is completed.

Mr. Steinberg asked about GASB's continuing involvement because he did not see much divergence between state/local and federal issues. Ms. Payne noted that GASB was providing input to AGA regarding the research.

Mr. Dacey noted that the International Public Sector Accounting Standards Board discussed the topic but had not added a project. It remains unclear what the standards-setters role is relative to electronic reporting. He thought the best thing that could come from the AGA research is best practices in areas such as how can you display information to maximize its usefulness. He was hopeful that AGA would produce a comprehensive and thoughtful report and useful recommendations. He particularly emphasized the need for communications experts to address things like display options. He thought there was a need to address integration of the transparency information. AGA is also working on notions of how to put financial information together to benefit users— from the transaction data level to highly aggregated information.

Mr. Granof noted that the GASB had a very similar discussion. He noted that he had ranked the project very highly but has since changed his mind. He doesn't see standards coming out in this area. However, he thought the AGA project is very important. In standards-setting, he thought we should take advantage of opportunities to encourage electronic reporting. For example, he thought requiring statement preparers to link amounts reported with supporting schedules is possible; although it raises audit issues.

Mr. Allen suggested the discussion turn to priority setting and the questions raised in the staff memo. Ms. Payne pointed to the options listed in her memo and asked members for their input on the options.

Mr. Jackson noted that the survey results included a comment that current projects don't align with the critical needs of the federal financial management community. The Board ought to talk about how information it requires can be useful. Some still argue that the information does not pass the cost-benefit test. He believes information required by standards meet critical management information needs. He thinks there should be an analysis showing how the information can be used. He disagrees with the assertion that the CFO Act has not produced meaningful information; for example, budget information has improved dramatically as a result of the CFO Act. At OMB, he started a project to show how to use financial information but was not able to finish it. Such a project would be very helpful since one does not know how to use something if one has not been trained or educated to use it. Such an effort would improve the responses we receive to proposals.

Mr. Allen asked if early members went through similar discussion on why certain financial information needed to be reported as they did at GASB. For example, he explained that state and local infrastructure was not to be reported in early deliberations but ultimately the members realized that you needed infrastructure information to balance against the liability incurred to finance the asset. Otherwise, net position is not correct. However, GASB did make it easy to report infrastructure by allowing estimates for existing infrastructure.

Mr. Steinberg said the big difference is that FASAB was not talking to accountants while GASB was. Mr. Jackson also noted how fast the FASAB was expected to act in the

early 90's. He referred to the 18-month deadline for producing cost accounting standards imposed under the National Performance Review.

Mr. Granof mentioned the GASB users guides. They aid different types of users in understanding and using state and local financial reports.

Mr. Dacey noted that GAO has produced a publication about how to understand financial statements. It does not go to the level of detail of a particular line item but focuses on each financial statement. [Note: the publication is entitled "Understanding the Primary Components of the Annual Financial Report of the United States Government" <http://www.gao.gov/new.items/d09946sp.pdf>].

Mr. Granof noted that the standards also impose discipline on the agencies.

Mr. Dacey noted that it was important to make sure the three- to five-year plan is communicated. We ought to give people an opportunity to tell us if they disagree with our priorities. The Board has reasonable ways to identify issues. He doesn't see a need for forums or public comment periods on proposed agenda items.

Ms. Kearney agreed with Mr. Dacey. It would be helpful to give the community a chance to look at our priorities. She thought it should be left open so that the community could have a chance to say what they need help with.

Mr. Reger indicated that Treasury has gone a long way toward electronic reporting but still has a long way to go. The community is moving to electronic reporting with all due speed. If it requires changes in standards, the Board would need to act quickly. On the issue of communicating the plan, perhaps the Board should use electronic means to communicate its priorities and allow them to comment back. Also, a small annual planning process is helpful.

Ms. Payne indicated that she would develop a way to communicate the plan and send it to members before the next meeting. Also, an annual planning review would be scheduled.

Ms. Payne moved to the topic of resources. She asked if members wished to express a consensus view on resources or to suggest to the steering committee that other funding mechanisms be supported.

Mr. Showalter indicated that resource constraints do impact what we are able to get done. The annual budget has gotten smaller over time. He noted that the budget of the whole organization is small relative to the budgets of the agencies funding the Board. The limitations on resources constrain our use of contractors and how we approach issue resolution. His concern is that the agenda is developed around the budget rather than the agenda is developed followed by the budget to achieve the agenda.

Mr. Granof added that it is important that the annual report do more than just say that we've responded to the budget cuts. We should also use the annual report as an opportunity to advocate for increased support.

Ms. Kearney said OMB took a different perspective. She thought it was important to see what issues are absolutely burning that need to be addressed. Viewed in isolation the fact that the resources were reduced was not a concern. She asked what standards absolutely have to be issued to allow agencies to produce their financial reports. Being at a more mature place now in comparison to the 90s, she thought the demand for standards has diminished but she does not know for sure.

Mr. Dacey indicated that he focused on the three- to five-year plan and it guided him in considering resource needs. There are project plans to complete those projects timely. After the discussion of the project plans presented for this meeting, he would like to discuss resource needs with the sponsors.

Mr. Steinberg thought the recent federal budget discussions were telling—there were many competing numbers (such as the CBO and OMB projections). In the final analysis, the financial statements show what actually happened. You need to have standards to get reliable financial information. He pointed to the shorter meeting schedule as evidence that there is not enough funding to support two-days of deliberations.

Mr. Granof indicated that the financial crisis in 2008 led to new types of transactions but we won't have standards ready until more than five years after the crisis. Mr. Showalter indicated that he thought the project plans were too long—perhaps due to a shortfall of resources.

Mr. Reger said he hoped the sponsors have approached this well – the Board spent more time on the three- to five-year plan this year than in past years. Other standards-setters also have long lists of potential projects that they can't yet get to. This is an indication of more than just financial resource constraints – it also considers deliberative time, the ability of the community to respond to proposals, and what could be implemented in a timely manner. He noted that there is a lull in demand right now. He believes it won't be a long lull; things will come up. As long as we annually revisit what needs to be done he is not concerned. He indicated that Treasury sees sufficient value in what this organization brings to fund it but noted there will always be give and take in a government setting between resource providers and resource consumers.

Ms. Kearney noted that she thought the project plans were long but did not see that as being due to resource constraints. Instead, it seemed driven by the collaboration and alignment sought. She suggested finding efficiencies in the process.

Mr. Schumacher commented that our latest consultant did a terrific job and we are now unable to bring in experts to assist. He doesn't like to see us miss opportunities to rely on outside experts. It would seem faster than relying on task forces to gain expertise.

Mr. Allen said he didn't believe funding levels impeded us during the last year. He is concerned going forward though. The discussion of how to shorten the timetables is important. He noted that FASB has a huge staff and reporting entity has been on their agenda for years. Often, how long a project takes depends on the complexity of the project. Flexibility to bring in experts would be good. He thought the discussion of the project plans would help us understand the resource needs. Risk assumed is so complex that it has the potential to take several years.

Mr. Steinberg asked what the alternative funding sources might be. Ms. Payne offered two examples – a fee tied to audit contracts and a collection from CFO Council members. She noted that in any case the organization would need a budget to authorize use of available funds or to set fees.

Mr. Steinberg asked about donations. Ms. Hamilton explained that the agency would need to seek gift authority in legislation.

Ms. Payne indicated that the annual report will include a summary of each perspective on the adequacy of resources. Absent a decision to ask the steering committee to seek another source of resources, the annual report would be silent on that option.

Mr. Showalter indicated that he was satisfied with the wording in the annual report. His concerns focus more on the future. He believes it is important that the non-federal members continue to monitor the resources and to speak up about concerns.

Ms. Payne noted that she believes staff can continue to increase the use of outside resources and in the interests of time she would move to the next issue. Mr. Schumacher encouraged efforts to bring in interns.

Mr. Reger noted that the OPM is forming an intern program for CFO staff. It would be similar to the presidential intern process. The goal would be to move them around and gain a multi-agency base. He also acknowledged that such arrangements would be short-term and not as helpful for long-term project management.

Mr. Allen indicated that he did not support any change in the meeting schedule. He favors efficient operations but believes quarterly meetings allow too much time for members to forget prior decisions. Mr. Schumacher agreed and encouraged continued use of emails between meetings. No other members commented on the meeting schedule.

Mr. Allen also noted that Mary Foelster, from the AICPA, was observing and could offer input directly to Ms. Payne.

Ms. Payne introduced the next topic-distribution of briefing materials. She noted that electronic distribution as materials are completed might be helpful. Alternatively, accelerating the dates for hard copies could be considered.

Mr. Showalter noted that his concern is that member feedback to staff should be earlier rather than later to be helpful.

Mr. Jackson asked if electronic files could be other than a single large PDF file per project. He is reluctant to print the entire package and can not easily insert comments in a PDF file.

Ms. Payne agreed to send Word files for the draft documents. Moving on to the decision of what to include in first and second distributions, she asked that staff judgment be permitted to continue so that time is available as needed to consult with task forces before sending more complex materials. Members did not object.

Ms. Payne noted that the next concern is that major issues be discussed and resolved before a pre-ballot is presented. She asked for member input. Members offered no further comments.

Ms. Payne indicated that the question of drafting an exposure draft (ED) before major issues are resolved should be discussed. Mr. Allen indicated that staff believes the Board focuses better when material is presented in a draft exposure draft. He wondered if simply putting the issues in the form of draft standards language created a problem.

Mr. Dacey indicated he was not troubled by the current process. He acknowledged that members do read the draft ED several times but believes it is helpful. If we waited until we thought we had resolved all the issues before preparing a draft ED, then the process would be longer.

Mr. Showalter agreed. He thinks it is helpful to see the language in the form of a standard.

Ms. Kearney thought it was helpful to see what we agreed in the form of an exposure draft. She asked if we could see the track changes only from the last draft rather than from the life of the ED. Further, if we went to fully electronic, we could get three versions – clean, changes from the latest version, and changes since the very first version.

Mr. Reger noted that the process of building something requires you to look at what you're building.

Ms. Payne explained that some federal advisory committees are using WIKIs. The public due process requirement is met by allowing the public to see the draft evolve online. In such a system, the members could have access through a password system to edit the document and insert comments. The public can then view the edits from members but can not edit the document.

Mr. Allen noted that you lose a bit when you go to online deliberation and editing. The online dialogue is different than in person. He thinks the credibility of the resulting document is questionable. He did not think a WIKI should be used to address concepts but could be used to edit final documents.

Ms. Kearney explained that she found WIKIs useful but agreed it could not replace the Board meeting face to face. The WIKI could enhance the editing process.

Mr. Showalter noted that if some members used it and some did not that could pose a problem.

Mr. Reger noted that once you start doing the editing online members have to keep up. In person meetings force members to pay attention to the dialogue—good ideas or significant edits might be missed.

Ms. Payne suggested experimenting with a task force first.

Ms. Payne noted that she has had some comments from members on the draft annual report. In the interest of time, she explained that the draft annual report will be circulated again before the October meeting and slated for approval at the October meeting. If members have additional input on the August draft they should send it via email or phone call.

**CONCLUSIONS:** The following process improvements were agreed:

1. the three- to five-year technical agenda will be communicated as a stand along document and include an explanation of how to submit any suggestions to the Board
2. the Board will annually review its technical agenda
3. the executive director will pursue opportunities to use outside resources such as interns
4. members will receive Word files for each draft document to facilitate feedback to staff

- **Federal Entity**

Staff Member Ms. Loughan began the Federal Entity session by explaining that two briefing packages had been distributed for the Federal Entity project for the August meeting—Tab B1 addresses government-wide issues and Tab B2 addresses the next phase, Component Entity.

Staff explained the primary objectives related to the government-wide issue is to review staff recommendations and approve the staff proposed language for the consolidation of FASB-based information without conversion and the revised disclosure language about non-core entities', specifically incorporating an example for referring to separately published financial statements. In addition, staff would also be seeking approval on the changes made to ensure consistency in language regarding how we present entities included in the report versus those consolidated as a core entity.



Staff directed the Board to the first issue “Develop Guidance for the Consolidation of FASB-based Information without Conversion.” Staff explained at the June meeting the Board decided FASB-based information can be consolidated with FASAB amounts with a disclosure of the accounting policies as needed. Staff explained it was agreed line items would reference disclosures breaking out the numbers where there are material policy differences and describing the accounting policies used. The Board also agreed the disclosure would not reconcile or show the differences between the two GAAP based amounts. No amounts would change (other than as a result of eliminations) in preparing the consolidated government-wide statements.

Staff had prepared Draft language for the standard, Basis for Conclusions and a Question for Respondents based on the concerns raised by a member. Ms. Loughan opened the discussion for Board member questions and feedback on the issue.

Ms. Kearney (OMB Representative for Ms. Bond) explained there were some inconsistencies noted in the language as at times there were references to disclosures for material differences and others for significant differences. Staff noted they would review the language to ensure it is consistent.

Mr. Schumacher noted at the bottom of page 3 it references that SFFAS 34 allows certain entities to prepare financial statements in accordance with FASB standards and asked who ultimately makes that decision. Staff noted that there is some guidance in SFFAS 34 but it permits those federal entities currently applying financial accounting and reporting standards issued by the Financial Accounting Standards Board (FASB) to continue to do so. SFFAS 34 also clarifies that a federal entity preparing GAAP-based general purpose financial reports for the first time is required to implement FASAB standards unless, in consultation with its auditors, the entity clearly demonstrates that the needs of its primary users would be best met through the application of FASB standards. Staff noted that the ED may provide an excerpt of SFFAS 34 if the Board believes that would be helpful.

Mr. Reger directed the Board to page 5 and explained he was trying to determine how the display ultimately would look. He wondered if the amount was by organization. Staff explained it is the total amount for FASAB and the total amount for FASB for the particular line item. The list of entities is just to identify those entities preparing per FASB, but no amount is required.

Mr. Dacey asked if the list of entities would be for all entities or just significant ones. Staff noted that materiality provisions apply, but it appeared in the case there would be a limited number of specific FASB entities as the disclosure only applies to listing the FASB based entities. Mr. Dacey also noted some concern with how the word “material” was used in par. 3 on page 5 and he noted it should probably be more related to material FASB amounts. He explained that if there wasn’t a material FASB based amount, then there probably wouldn’t be a need to disclose it. Mr. Dacey added that it is applicable to any line item where there is a material FASB amount. Mr. Dacey

explained the focus is on whether the FASB based amount is material to the particular line item, then one must disclose the accounting policy and amounts (in total between FASAB and FASB.)

Chairman Allen explained he interpreted it slightly different. His interpretation was that if the two policies resulted in the same amounts then one wouldn't have to disclose the differences. Mr. Dacey agreed that there may be situations where two different policies are used that may not result in different amounts—for example, investments at fair value.

Chairman Allen explained he thought the disclosures only kicked in if there were significant differences in amounts under the two methods. Mr. Reger noted that in essence, we are still requiring a calculation to know the difference. He added he thought the goal was to say the different standard is acceptable and simply disclose the dollar values of the line items. Mr. Jackson explained that we didn't want to require the preparer to have to make those calculations or determinations of differences. He added we wanted to avoid the separate analysis and conversion. Mr. Jackson explained the Board agreed it was acceptable to state for a particular line item this amount was FASAB based and this amount was FASB based. Mr. Jackson stated this would enable the reader to know they are accounted for on a different basis. Mr. Dacey explained the disclosure would also include the accounting method or valuation. Mr. Jackson explained he doesn't see what the calculation is, basically if one is preparing based on FASB that amount is disclosed.

Mr. Dacey agreed and stated no one would be required to do a conversion calculation. The question is if the FASB based amount is material to the line item, then one must tell the reader \$XX is based on FASB and \$XX is based on FASAB. Additionally, the accounting policy for each is disclosed. Mr. Jackson explained it doesn't require any burden on the preparer at the agency level. Mr. Jackson noted the decision is made by Treasury upstream based on whether the FASB amount is material in relation to the total amount.

The Board expressed concern with wording of the paragraph. The Board agreed with what Mr. Dacey and Mr. Jackson conveyed and wanted to ensure the wording articulated it.

After discussion, the Board tentatively agreed to the following:

“the following disclosures are required where the FASB amounts are material to the line item and there is a difference in accounting principle or standards” Mr. Jackson noted that having this as the introduction then subparagraph a.) works as is “descriptions of the different accounting policies and methods applied and the related amounts included in the line item.”

Chairman Allen asked if there was a duplication of what is included in the basis of accounting note. Mr. Dacey explained it could be included in the basis of accounting

note or with the particular line item note that it is supporting. He views it as flexible and not something that would be duplicative.

Mr. Showalter asked how many line items this might have an impact on. His concern was he didn't want to see it cluttering the consolidated statements anymore than they already are. Mr. Reger explained he didn't believe it would affect a lot of line items or result in a huge change.

Mr. Jackson noted concern for subparagraph b.) that requires the identities of specific component entities that reported FASB based information. He questioned if the information was necessary and noted it may result in a laundry list of information. He noted that although materiality kicks in, he isn't sure it is necessary to hi-light that information. He noted the phrase "identities of specific component entities" is tricky and wondered if something along the lines of principal component entities included in the consolidated report. Mr. Dacey suggested component entities that reported significant amounts. Mr. Jackson explained the point it should capture is that components should be disclosed where the information herein has been presented separately. The point is we don't want to require every entity to be listed.

Staff noted that the sentence in par. 3 sets up the parameters first, so not every entity would be listed. The Board agreed it would only be the FASB amounts that are material to the line item, so that must be met before sub-paragraphs a.) and b.) are required. Mr. Jackson agreed but stated it should be clear so that it is not misinterpreted so that every entity must be listed. Staff agreed. Mr. Jackson explained it could state it is those entities that contribute significantly to the line item, or actually one could solve it by stating if it contributed significantly to the separately reported amount. He explained one knows that materiality plays into this as well, so naturally it would meet that threshold.

Chairman Allen suggested that staff develop language that would capture what had been conveyed and seek approval at the next Board meeting. Staff agreed and noted the focus would be on material FASB amounts and ensuring the language is clear that only those that contributed significantly to the separately reported amount are required to be listed.

Chairman Allen noted that on page 6 the question posed for respondents stated: "One member believes that the preparer should be permitted to convert any FASB based information to FASAB based information if considered necessary for fair presentation." He explained he realized that it was his position and after reading the minutes, it appeared other members agreed the question should be asked. Based on discussion, it appears the Board members are in agreement there shouldn't be a conversion. He noted OMB has brought up previously that there are legal concerns if different amounts were reported for certain entities in two different places. Chairman Allen explained based on this he would like to retract the question.

Mr. Showalter explained he understood Chairman Allen's concern, because in essence by providing this in the standard, we are prohibiting the conversion to FASAB and taking the judgment away from Treasury. He questioned why the Board would want to do that. Mr. Dacey explained it would present pragmatic challenges if you had some of the entities converting to FASAB and some of them that didn't. It could be very confusing and a preparation burden.

Chairman Allen explained he would withdraw the request if the flexibility is not something that Treasury wants or needs. Mr. Reger explained that it might add complexity. Therefore, Chairman Allen stated he would withdraw the question. Mr. Dacey explained we should ask if they agree with the Board's position that there should not be any conversion of the data and if they don't agree, they should provide an explanation as to why and provide another alternative. Mr. Reger explained he doesn't want there to be a choice as to whether an entity converts or not for purposes of consolidation. Chairman Allen directed staff to drop the question drafted and instead include a broader question about whether respondents agree with the Board's position that there should not be any conversion of the data.

Ms. Loughan directed the Board to the second issue "Revise the required disclosures regarding non-core entities, specifically incorporate an example for referring to separately published financial statements." Staff explained the Board requested staff to include a reference to non-core entity financial statements in the examples for non-core disclosure requirements and to clarify that the items listed in subparagraph a.-d. are examples of information that may be disclosed and are not specific requirements.

Staff explained the reference was added to the list of examples and the preamble to the list of examples was revised so it was clear the examples are not required. A footnote brought additional clarity the examples were not required as it stated "No individual example is itself a required disclosure. Therefore, the examples are not alternatives or substitutes one for another. Instead, a disclosure that provides an understanding of the potential financial impact should be provided." Ms. Loughan opened the discussion for Board member questions and feedback on the issue.

Mr. Steinberg noted the change was clearer on these are examples and not requirements, but he believed the geography could still use adjusting. He noted the first one listed was summary financial statements and he didn't want to see the CFS inundated with summary financial statements. As of now, we are not including summary financial statements for any entity, so he doesn't see why we would. In addition, the key information we are looking for regarding these types of entities is what is the risk and potential financial burden to the federal government coming from these types of entities and that should be listed first. He explained readers might not be able to interpret summary financial statements and gather the information necessary from them versus a few sentences conveying what the risk and potential financial burden is to the government. Therefore, Mr. Steinberg suggested moving c. and d. up in the list of examples information.

Chairman Allen explained he didn't oppose the change in geography, but he did support maintaining the summary financial statements in the list of examples because there may be an instance where that information may be important. For example, if one decides the Smithsonian isn't consolidated then one may be concerned about the financial health of that entity and summary financial statements may be important. Mr. Steinberg explained that seeing summary financial statements may not always explain all the information.

Mr. Jackson explained he had concern with par. 3 and 4 on page 8 of the staff memo. He noted par. 3 states:

"For any core government entity transactions with the non-consolidated non-core accountable entities (which are accounted for by the core government entity in accordance with the GAAP hierarchy established in SFFAS 34), a summary of amounts reported in the core government entity financial statements and the basis for determining the amounts reported."

He explained this creates a huge burden as the core entity must report the transactions with the non-core entities. He believes this is a huge disclosure requirement.

Chairman Allen explained it wasn't transaction based as it stated the "amounts" reported in the financial statements. Mr. Dacey noted he had some concerns as well but perhaps it might need to be reworded to be clearer. Mr. Jackson noted concern with "transactions" and believed that should be revised and the fact this information has to come up stream creates a huge burden on agencies and a significant requirement.

Chairman Allen explained he believes what is important is information such as total balances derived from many transactions rather than amounts for individual transactions. Staff noted that the language may need to be revised to be clearer. Mr. Dacey noted that he isn't opposed to amounts arising from transactions being included; he just wanted to be clear that it might expand what is being disclosed. The challenge is ensuring the language is appropriate so we don't unintentionally expand disclosures. Staff noted the materiality provisions would still apply and it wasn't the intent to include individual transactions. Mr. Jackson explained he wasn't arguing that something shouldn't be disclosed he was more concerned with the burden on agencies and the clarity of the language.

Mr. Steinberg reiterated he is more concerned with the risk to the federal entity, the details of the transaction about the events that have happened aren't as important. Chairman Allen explained he believes there is importance to information such as the total investments in a particular non-core entity.

Mr. Jackson explained that par. 4 states

"The amount that best represents the federal government's maximum exposure to gain or loss from its involvement with the non-core entity, including how the maximum exposure to gain or loss is determined. If this cannot be quantified, that fact should be disclosed."

He noted the notion of "maximum exposure to gain or loss" should be explained further. He stated this gets back to risk assumed as it may be something we can't say anything about or quantify. Mr. Jackson explained this is a critical paragraph and there doesn't

appear to be a lot of explanation to it so it leads to confusion with par. 5. Mr. Jackson explained that he thought pars. 3 and 4 required some clarification.

Ms. Payne explained par. 4 does state that if maximum exposure can't be quantified, disclose that fact. She also noted that par. 3 and 4 are both necessary for example with Fannie and Freddie—the Investments are reported which satisfies par. 3 but the maximum exposure to risk or loss is very different which would satisfy par. 4.

Ms. Payne asked if the Board wanted staff to write about acceptable methods to measure maximum exposure. Mr. Jackson explained if the federal government created an entity then it may need to be looked at in a macro sense versus a micro sense. He explained the federal government may create a non-core entity but the principal business of that entity creates a risk that the federal government may need to explain. Mr. Jackson noted that par. 4 should explain this whereas par. 3 is more at a micro level where it discusses transactions and balances between core and non-core entities. Staff noted the language could be improved but this is for material balances at the government-wide level and all of it was supposed to be at a high level.

Staff noted the word “transactions” may have caused issue but there was a problem with people understanding these are events that have already taken place, and these have been captured so tell us in the aggregate what that amount is. Chairman Allen explained if for example half the receivables are with a non-core (unconsolidated) entity that would be important to know.

Mr. Granof noted that in standard setting, one starts with the general then move to the specific—one sets standards then apply them to specific or individual entities. He noted that doesn't appear to be what is happening. The focus shouldn't be on entities like the Smithsonian, it should be on the big entities. The critical issue should be how entities will be disclosed and it should be on a continuum with more disclosure versus less. Mr. Granof noted that yes, you would want the risk disclosed but for some you would also want the transactions or balances disclosed because for some of the non-core entities, they are much more “core” like than non-core.

Mr. Jackson explained he believed the primary focus should be on the risk, though he believes the transactional data may be indicators or reinforcements of the heightened risk. He added that perhaps the order of the paragraphs 3 and 4 need to be reversed and it may bring more life to par. 5.

Mr. Steinberg explained that some of the confusion may have resulted from the change from the original definition of several different categories to now where we have one category called non-core. He explained perhaps we need to revisit the previous thought of different groups where the disclosures would be different. Chairman Allen explained he didn't believe any of the Board members would question that the focus is on risk.

Mr. Dacey explained he supports par. 3 and the financial statements currently include this type of information for entities. He believed the information was important,

just as the information required in par. 4 that addresses future exposure. Mr. Dacey explained he was supportive of the general approach.

Mr. Steinberg noted that it probably depends on the type of entity—for some par. 3 information may be more important where for others, information for par. 4 may be more important. Chairman Allen explained he believed par. 4 and par. 5 were probably more important but he understood the value of the information in par. 3.

Mr. Granof explained it would be helpful if there were examples for each type of information and the type of entity it would be appropriate. Mr. Dacey noted it gets back to relevance and importance in the arrangements. He explained we disclose both, for example we disclose a gain or loss during a period and balances at the end of the period and the maximum amount of exposure as of the end of the period which may be different than the investment.

Mr. Showalter explained that par. 4 and 5 are very related to each other as par. 5 provides examples. Therefore he believes the order of the paragraphs is fine. Mr. Showalter also noted that par. 3 was necessary but for different reasons. Mr. Jackson explained he better understood the reasoning for par. 3.

## **LUNCH BREAK**

Staff asked if there were any concerns with par. 5 or the specific changes made. Mr. Dacey noted that he would reorder them. He thought it would be better to put them in order in which they were likely to occur—c., e., d. a., and then b. Mr. Dacey explained that he viewed it as 3 broad objectives that we were trying to achieve through the disclosures and perhaps the examples were types of information that would fulfill those three broad objectives in a flexible way. Chairman Allen asked if the Board objected to staff taking that approach.

Mr. Reger asked Mr. Dacey to summarize what the three objectives were. Mr. Dacey explained the three were the nature of the relationship, nature and magnitude of the activity during the period, and the future risks and exposures. Mr. Dacey added that the examples in par. 5 are examples for the three broad areas and some things may overlap and it could be a couple paragraphs that integrated the information.

Ms. Loughan directed the Board to the final government-wide issue presented “Review Draft ED for consistency in language regarding how we present entities included in the report versus those consolidated as a core entity.” Staff reviewed the Draft ED and modified the language accordingly to address concerns related to the wording of entities included in the report versus the entity to ensure consistent throughout. Staff noted the tracked changes were included in the Draft ED. Ms. Loughan opened the discussion for Board member questions and feedback on the issue.

Mr. Steinberg explained that he believed the interventions required substantial disclosures but he doesn't believe we should be calling them non-core accountable

entities because with that label it sounds like they are part of the federal entity. He noted that they are not accountable to the federal government. Chairman Allen explained that for some we own over 50% of stock so it is difficult to see how they aren't accountable when the government owns the entity. Mr. Steinberg agreed that we own the stock, but that is because of the bail-out circumstances and that doesn't make them accountable to the Federal government. Therefore he had concern with calling them "non core accountable entities." Chairman Allen asked if he had a better term. Mr. Steinberg explained he would simply call them "intervention entities," in a class by themselves. Mr. Jackson noted that it might be non-core accountable entities had to be something that the federal government created versus saved.

Mr. Steinberg explained that at an earlier stage in the project, there were four groups of entities but now there are two—core and non-core accountable. Staff noted there are still the types of classes noted within the non-core to assist the preparer in making the determination, which includes the Interventions. Staff also noted that they probably aren't going to be labeled "non-core accountable" in the disclosures or financial statements, it is a way to make a distinction, but it is not required to be labeled in any particular format. Staff explained it is a fluid bucket of non-core. For example, look at Amtrak—and how long would one consider it to be temporary intervention. Mr. Steinberg stated Amtrak should be non-core since it was established by the Federal government and the Federal government owns 100% of the stock. He also explained he has concern with calling the intervention entities accountable when he doesn't believe they are accountable.

Ms. Payne suggested the word "accountable" could be dropped for brevity as at times we refer to them as simply non-core. They share the characteristics of the other non-core entities, so staff is not certain why there should be a distinction or a need to exclude from non-core. Chairman Allen asked if there were different disclosures required for them? If so, then he may understand having a different grouping but if the disclosures are the same then he doesn't understand making a different group. Mr. Steinberg noted that the distinction is the fact that these are private sector entities where the government intervened. Chairman Allen noted there are receiverships with private banks as well.

Mr. Steinberg agreed the disclosures may be similar or even the same, but he doesn't believe the interventions should be called non-core accountable entities, it infers the federal government sets them up. Mr. Dacey asked if it would be more appropriate to simply call them non-core as staff suggested earlier. Mr. Reger agreed it might address Mr. Steinberg's issue, if the word accountable was dropped. Mr. Jackson noted par. 42 that describes non-core accountable entities states "federal officials may rely on organizations that have a great degree of autonomy...." The Board believed that language needed to be revised to include others they may get involved with. For example, later paragraphs (49-51) include the specific references to the examples of types of non-core.



Mr. Dacey noted he had concerns with the word “rely” as well and would prefer that to be revised. He noted that our involvement in some of these were to achieve public policy objectives, such as preserve the economy. Mr. Reger noted that we do identify Federal Government Intervention Actions as a type within the non-core. Mr. Reger asked Mr. Steinberg if that specific identification wasn’t enough within the non-core. Mr. Steinberg explained he didn’t believe they should be included as non-core.

Staff noted it would be an exception. Mr. Showalter explained you would, in essence, be splitting it into a third category, but then bringing it back together because the disclosures would be the same. Mr. Steinberg suggested this category be for those actions related to private companies where the federal government intervenes to preserve jobs, preserve the economy, etc. Ms. Payne explained similar language was included in a previous draft and the Board collectively looked at it and said it was an exception.

Chairman Allen explained that if Mr. Steinberg had a specific proposal on wording then he could present it to the Board for discussion and vote if he chooses. At this point, he suggested the Board move on to the second paper.

Ms. Loughan directed staff to the second briefing paper B2 –Component Reporting Entity. Staff explained the primary objective for Tab B2 is to review options and approve the approach to the component entity phase of the federal entity project. Staff recommends the overall framework for the component entity standards should be the same and generally consistent with what has been established for the government-wide (principles for inclusion in the component entity and consolidation). Staff noted the paper detailed FASAB’s current pronouncements and previous Boards have concluded that the same objectives apply to both component and government-wide reporting entities and that all costs and liabilities reported in the government-wide must be attributable to a component entity. In addition, there appeared to be a general notion and principle that all costs and liabilities must be reported at the component level before flowing into the consolidated statements.

Staff noted the paper explained the principles for defining what organizations should be included in the component entity reports should be consistent with those established for the government-wide. Principles and attributes established for core and non-core entities would generally be the same, but would have to be revised to fit the component entity level versus government-wide. For example, the component entity core accountability would be with Top Level of Management or the Component Reporting Head (or equivalent) with a span or scope of accountability that includes organizations in the budget instead of “accountability that rests with President and Congress” as in the government-wide. In addition, non-core accountable entity disclosure requirements for presentation in component entity reports should be the same as those agreed upon as required in the government-wide. Naturally, based on materiality, the information presented in consolidated financial statements typically is aggregated and in less detail than in component entity financial statements. Therefore, when considering the entity reports, it may mean that certain non-core accountable entities may meet materiality

thresholds in component entity reports while not in the government-wide so that disclosures are more extensive in component entity reports. Ms. Loughan opened the discussion for Board member questions and feedback on the issue.

Mr. Reger asked if everything would be repeated in the component entity section. Staff noted there appeared to be enough differences in terminology where it wouldn't appear to be a verbatim repeat.

Mr. Dacey explained he generally supports the government-wide approach, especially in deciding what is core and non-core. At the component level we have the question of what is included in the reporting entity for meaningful presentation. He noted that in our concepts statement we noted that sometimes in the federal government, assets and liabilities are assigned to an entity based on various criteria. In addition there may be component entities that have odd responsibilities assigned and may not be complete because of the relationship they have with the parent entity. Therefore he viewed it slightly differently and would ask whether an entity provides a complete picture of its operations versus going through the core and non-core questions and other principles. Instead he believed it might be slightly different questions for a component entity and what makes it complete. Mr. Dacey explained that classifying an entity as core or non-core should be consistent across the government.

Staff explained she was framing it more in line with the inclusion principles—budget, ownership, and control. Mr. Dacey explained he believes there may be additional disclosures required to describe other things related to the component entity. He offered the example of the Senate restaurant and how that was disclosed in the financial statements. He explained that with component entities there are interesting combinations and ways that they are carved up so there may be questions as to what is a complete economic activity.

Chairman Allen asked Mr. Dacey what his proposal was. Mr. Dacey explained it may be more of a question than a proposal. Mr. Showalter explained he thought staff was suggesting to start with the same principals then determine if there are additional questions that need to be asked. Mr. Dacey offered the example of whether the Department of Labor (DOL) would include the Pension Benefit Guaranty Corporations (PBGC) to be complete, these are the types of things that would need to be worked through. Staff recognized there are some unique obstacles that may need to be addressed at the component level. Mr. Jackson recognized that the boundary issue becomes more important as one goes upstream, for example—PBGC can issue a stand alone report, but Department of Labor can also issue a report. The question whether smaller components are within your reporting entity becomes complex for components. Mr. Dacey explained staff had noted in the paper one way to determine what organizations to include would be to look at organizations for which the top level of management or the component reporting head is accountable for.

Ms. Kearney noted PBGC had previously requested that they be directly consolidated in the government-wide and not with DOL. They made the request because they believed,

although they were listed under DOL in the budget, the budgetary relationship with DOL was an administrative type relationship with DOL and not one related to control or direct accountability. Ms. Payne noted the standards could provide for situations such as this at the components level- it could provide principals based criteria as to what components are accountable for and should be included in the report. She noted there wouldn't have to be an OMB waiver if the standards provided criteria that addressed it.

Chairman Allen noted that there would be unique situations that applied at the component level and at this point we need to decide if the government-wide is a starting point. He noted that several members appear to think that they would be the same, does that appear to be sufficient? Mr. Dacey explained the key question is which core entities do you have to include in your report for complete presentation. Mr. Jackson noted one could state it is everything under the Secretary's or Department head's accountability. Mr. Steinberg stated he believed the criteria for the government-wide should be the same for the components but he also believes that the accountability at the component level should be straight forward to the head of the agency. Mr. Dacey noted it would be most of the time, but sometimes it might not be clear cut, for example with PBGC.

Mr. Dacey explained we needed a principles based solution. Options might include whether it is under the control or authority of the department head or based on more general or broad flexible principles. Chairman Allen noted it might be an expansion of the government-wide principles.

Mr. Reger explained there are 149 entities coming into the consolidated. Therefore there needs to be a standard guiding the preparation of these statements. Chairman Allen noted there could be various levels in the federal government. However there needs to be a basic framework and staff will work on developing that for the Board's consideration.

**CONCLUSION:** Staff will prepare revised wording on the Consolidation of FASB-based information for the Board's review. Staff will also prepare a revised disclosure section for non-core entities that focuses on three broad objectives and examples of information that support those three objectives. Staff will develop more detailed options on the component reporting entity approach for the Board's consideration.

- **Reporting Model**

### Overview

Mr. Simms presented a project plan to review the reporting model for component entities. Board members discussed the focus of the project and the need to ensure that the project includes input from managers and citizens. Staff will enhance the plan to address the Board's comments. Details of the discussion follows.

## Discussion

Mr. Showalter noted that the project should obtain input from citizens and he was concerned that the plan presumed that a statement of spending was needed. The focus should be on what information users need and how it should be presented. During discussions with users, the project may determine that a statement of spending may not be needed. Mr. Dacey noted that the project could utilize the information we have already obtained, such as the citizens and managers user needs studies and other sources.

Mr. Granof was concerned that the project was too broad and would require considerable time.

Mr. Steinberg noted that managers are the primary users of the component level financial statements and the project should focus on how to improve the statements for their use. While financial information is important at the government-wide level, performance information is important at the component entity level. Mr. Steinberg also noted that FASAB conceptual guidance, Statement of Federal Financial Accounting Concepts (SFFAC) 2, *Entity and Display*, calls for a statement of performance measures. Presenting performance information was being accomplished when agencies presented Performance and Accountability Reports which included a performance section. However, agencies are currently moving toward Agency Financial Reports which do not include a performance section.

Mr. Allen agreed and noted that the Board prepared a Strategic Directions report which noted that when citizens want to know how well the federal government is performing they look to the government-wide financial statements. However, internal users, like managers and legislators, are considered the primary users of agency reports. The project needs to consider how we can meet the needs of those users.

Mr. Jackson noted that, without any preconceived notions regarding the model, the project should consider the needs of managers – what do they use and what could they use if they knew how to use it. It would be interesting to know what acquisitions managers, logisticians, material management personnel, and others use to manage their programs and whether the feedback would change what is currently being reported. Preparers and auditors are not necessarily users.

Mr. Showalter noted that input from citizens is needed to determine what information should be consolidated into the government-wide report.

Mr. Reger noted that the Chief Financial Officers Act was intended to help managers obtain the information they need. Managers need information timely and they need that information to be accurate. They also need that information to be relevant to the decisions they need to make. He was not sure that consolidated financial statements for an agency or the government-wide meet those needs. Also, users want information

by topical area rather than by agency and we have not established those relationships. They want to know how much food safety costs and what homeland security costs regardless of which agency performs those functions. If the project will address this issue, it would be interesting, but it would be a long project. A long project may not make logical sense.

Mr. Granof noted that the project should focus on enhancing the shortcomings of the current model, rather than developing a whole new one. For example, members have noted the need for performance information.

Mr. Allen noted that it appears that Board members are not questioning the project, but have concerns regarding its focus. A revised plan could address: what information do we have now; what additional information would be needed; how the additional information would be obtained; the composition of the task force (to ensure that citizen and manager input is obtained); and the ultimate product. Mr. Allen encouraged Board members to email any additional comments to staff.

Mr. Jackson noted that it would be interesting to know what data managers use because, while it may not change the reporting model, it may change a particular standard so that there is linkage between what is reported and the data that managers are using. The project should make sure that managers are involved in the task force.

**CONCLUSION:** Staff will present a revised project plan at the October 2011 Board meeting.

- **Risk Assumed**

Staff member Julia Ranagan began the session by noting that the project on Risk Assumed was rated by the members as the number one priority project at the April 2011 discussion on the technical agenda. Ms. Ranagan stated that 1.5 FTE (full-time equivalency) have been assigned to the project; she would be spending all of her time on the project while staff member Ross Simms would work part-time as permitted by his ongoing work on the Federal Reporting Model project.

Ms. Ranagan reported that staff proposes to use a multi-disciplinary task force. As outlined in the proposal, staff would first develop an inventory of risk assumed by the federal government and then group those risks by similar attributes to give the task force something to start with. Staff would then utilize the task force to develop draft definitions, assess measurement issues and different measurement methods, and layout options for disclosure and required supplementary information. Staff would then present those options to the Board for consideration.

Ms. Ranagan noted that although staff would be using a task force to bolster resources, staff would involve the Board throughout, bringing issues to the Board's attention and

presenting options as they are being developed. Ms. Ranagan stated that staff plans to start with a broad scope as the Board agreed to at the planning session and narrow the scope as needed. She asked for feedback from members on the plan and proposed approach and whether members feel comfortable with it or have concerns.

Mr. Allen responded that he is very supportive and he thinks it is a very important project. He said he does not see it as a particularly easy project—he thinks it will be quite difficult—but the federal government probably has the greatest risk profile one could define because of its broad role and responsibilities.

Mr. Showalter said he supports the approach but he encourages staff to communicate with the Board often because it is something that is so broad, and the Board will probably want to communicate early and often on it. Ms. Ranagan acknowledged member concerns about the potential slippery slope so she plans to update the Board regularly to make sure staff is not going off track.

Mr. Granof stated that he believes staff is on the right track; the key is to identify the various types of risks ; then the determination to disclose or recognize those risks will fall right into place.

Mr. Schumacher said he was very supportive of the project and thinks the proposal is fine. He asked if the project would address inter-governmental dependency (e.g., states). Ms. Ranagan responded affirmatively.

Mr. Dacey said he is fine with the proposal but noted that there may be a slight overlap with work the Governmental Accounting Standards Board (GASB) is doing or thinking about doing and asked staff to inquire if there may be opportunities for potential coordination.

Ms. Kearney asked if there will be any overlap with this project and the Federal Entity project. Ms. Ranagan responded that there may be some overlap but staff will coordinate between the projects to make sure they are in sync and there is no unnecessary duplication.

Mr. Allen asked if there were any more comments and then wrapped up the session by stating that since there are no objections, staff should proceed with the proposed project plan and approach.

**CONCLUSION / NEXT STEPS:** Staff will begin preliminary research on the Risk Assumed project by developing an inventory of risk assumed by the federal government, a detailed task force plan, and a list of potential task force members.

- **Deferral of Technical Bulletin 2006-1**

Ms. Ranagan stated that the Board members' materials contained the comment letters received on the proposal to defer Technical Bulletin 2006-1, *Recognition and*

*Measurement of Asbestos-Related Cleanup Costs*, for one additional year as well as staff's analysis of the comment letters.

She noted that Mr. Showalter had expressed his intention to object to the final technical bulletin and asked him if he would like to share his opinion with the other members. Mr. Showalter responded that although this should not surprise the other Board members, he plans to object to the Technical Bulletin. He said he became even more convinced—after reading the comment letters and seeing that some of the agencies are just now doing surveys—that if the Board does not object to the technical bulletin, they will be having the same discussion next year.

Ms. Ranagan reminded members that at the previous meeting when the Board had agreed to expose the additional one-year deferral for comments, there were mixed feelings about granting the deferral. She noted that Mr. Jackson, while stating that he preferred to maintain the fiscal year 2012 effective date, had suggested that there would be no real harm done in providing one additional year for the agencies to finalize their methodologies as long as agencies that had already implemented or were in the process of implementing would not be negatively affected. She noted that the alternative was to do nothing because only one of the members had supported permitting the information to be reported as required supplementary information, as originally requested by the Department of the Interior.

Ms. Ranagan noted that the Board had agreed to propose the one-year deferral and the comment letters were overwhelmingly in support of the deferral, and she suspects agencies are already incorporating the anticipated deferral into their action plans. She asked if the other members had any comments on the issue. None of the other members raised any issues.

Ms. Ranagan responded that, if there are no further objections, she would send a revised draft to the members via email for a 15-day review period in which members can object before it is issued as final [technical bulletins are staff documents that can be issued if the majority of members do not object during a 15-day review period].

Mr. Steinberg inquired if there would be any changes from the draft that was in the Board materials. Ms. Ranagan responded that there would be minor changes to incorporate the one additional comment letter that was received after the staff analysis had been completed. In addition, Mr. Showalter had asked staff to incorporate its response to the comments into the basis for conclusions for the benefit of other agencies that may have the same questions.

Mr. Steinberg commented that he thought the summary of the roundtable was great; he thought it must have been extremely educational for the people that attended. Ms. Ranagan responded that it was one of the most useful meetings she has attended in government as far as the open and candid sharing of information; it was a very helpful session.

Mr. Steinberg asked if staff should host similar events for other contentious and technical topics. Ms. Ranagan responded that staff was planning to hold more of these events for technical standards and thought it would be a good idea to hold them sooner rather than just prior to implementation in order to allow for early and upfront discussion of issues.

Mr. Dacey said that the technical bulletin and several other recent statements have referred to general purpose federal financial reports prepared in conformance with Statement of Federal Financial Accounting Standards (SFFAS) 34, as opposed to being prepared in conformance with generally accepted accounting principles (GAAP). He asked if there was a reason the language was singling out SFFAS 34 as opposed to GAAP. Ms. Payne responded that she had not thought about it in those terms, noting that FASAB standards are read by individuals who may not be familiar with what GAAP is and that at least points them to the place where GAAP is defined. Mr. Jackson proposed that the language state "in accordance with GAAP as defined by SFFAS 34." Mr. Dacey agreed that would be a better way to state it.

Mr. Allen thanked staff and concluded the session.

**CONCLUSION / NEXT STEPS:** Staff will make the changes to the draft technical bulletin as discussed at the meeting and email another draft to members for the 15-day review period, after which time the final technical bulletin will be released if the majority of members do not object. Upon issuance of the final technical bulletin, the effective date for Technical Bulletin 2006-1, *Recognition and Measurement of Asbestos-Related Cleanup Costs*, will be for reporting periods beginning after September 30, 2012 (beginning in fiscal year 2013).

- **Leases**

Staff member Monica Valentine introduced the meeting materials at Tab F, noting that the proposed Lease project plan was prepared in order to get the Board's approval on the staff's approach to develop a new federal accounting standard on Leases. Ms. Valentine noted that the current lease accounting standards were developed in 1995 and included in SFFAS 5 *Accounting for Liabilities of the Federal Government* and SFFAS 6 *Accounting for Property, Plant, and Equipment*. When those standards were developed, the Board decided to use the high level language on lease accounting from Statement of Financial Accounting Standards 13, *Accounting for Leases*. She noted that the current federal standards only address the definition of a capital lease, the criteria for capital leases, and the measurement of a capital lease asset and liability. Between SFFAS 5 & 6 the capital lease guidance is minimal. Also, at that time, the Board had plans to use this guidance as a placeholder until the Board was prepared to add lease accounting to its agenda as a separate project. Ms. Valentine also mentioned that over the years, staff has received numerous questions about the lease standards primarily because they are not comprehensive and they do not make meaningful distinctions between capital and operating leases regarding the substance of lease transactions.



Ms. Valentine noted that staff's approach to developing a new standard on leases will include forming a task force of knowledgeable federal and non-federal participants who have relevant experience or interest in lease accounting within the federal government and evaluating the advantages and disadvantages of the new FASB/IASB lease standard in the federal environment. Staff will use the task force to gather data on current leasing practices throughout the federal government and to compile a comprehensive list of the lease accounting issues currently in the federal environment, especially those that are unique to the federal sector.

Ms. Valentine updated the Board on the current status of the FASB/IASB joint lease accounting project that began in mid-2006. The FASB/IASB Boards subsequently issued a preliminary views discussion paper in March of 2009 and later issued an exposure draft in August of 2010. The Boards have held numerous public roundtable meetings and educational workshops. Based on the results of the exposure draft comment letters, roundtable meetings, and Board deliberations, the FASB/IASB has decided to re-expose the revised lease accounting proposals. The re-exposure will give the community an opportunity to comment on the revisions to the draft since the August 2010 exposure draft was released. That new exposure draft is expected to be released sometime before the end of calendar year 2011. Staff estimates that the final FASB/IASB standard will be released sometime in the second half of 2012. In the meantime, staff will continue to follow the progress of the FASB/IASB project and will begin preliminary analysis once the re-exposed ED is released for comment. In addition, staff will begin to formulate a task force.

Chairman Allen asked staff what would be the plan if the FASB/IASB project got stalled or put off until a later time. Mr. Dacey stated that the Lease project was a high priority project for the FASB/IASB, especially since the Boards are converging on this topic. Ms. Valentine also noted that staff will begin preliminary analysis of their proposals once the re-exposed ED is available. Chairman Allen reiterated that at some point in the project the Board has to make the decision to accept the new FASB/IASB lease standards largely "as is" or to develop our own set of lease standards if the federal lease issues are so unique. Mr. Granof would like staff to provide information as to those areas where the leasing transactions/activities in the federal government are different from those addressed by the FASB/IASB lease standards. He also mentioned that GASB has just begun a project on leases. He also suggested that we coordinate with GASB on this project. Mr. Dacey agreed that the Board should look closely at FASB/IASB re-exposed ED and identify those areas within the federal environment that are unique (such as fiscal funding clauses) and possibly make adjustments to the FASB/IASB proposals to address those unique areas. Both Mr. Granof and Chairman Allen expressed their preferences to see all of the lease accounting standards between FASAB, GASB, and FASB/IASB align. There were no objections to the project plan presented.

**CONCLUSIONS:** Staff will proceed with the project plan keeping in mind the members' input.

- **Non-federal Investments**

Ms. Parlow began the discussion by noting that the briefing materials for Investments (Tab G) included a citation of the definition of “bailout entities” from FASAB Statement of Federal Financial Accounting Concepts 2, paragraph 50:

[50.] The Federal Government occasionally bails out, i.e., guarantees or pays debt, for a privately owned entity whose failure could have an adverse impact on the nation’s economy, commerce, national security, etc. As a condition of the bail out, the Federal Government frequently obtains rights similar to the authorities associated with the indicative criteria presented in paragraph 44. The existence of these rights does not make the bailed out entity part of the Federal Government reporting entity or any of the other reporting entities that are part of the Federal Government. Disclosure of the relationship(s) with the bailed out entity(ies) and any actual or potential material costs or liabilities would be appropriate.

She said that the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) are engaged in what is being called a “joint project” on investments, but that is actually more of a concurrent project, because the two standard setters are approaching the topic in different ways, with different timetables, and have not committed to issuing identical standards.

She said that FASB issued an exposure draft (ED) in September 2010, and has received over 2800 comment letters. The FASB ED proposes that a major class of investments (those being held for the collection or payment of contractual cash flows) should be reported as a reconciliation between fair value and amortized cost that would be presented on the face of the statement of net position.

She said that GASB and IPSASB also have reporting requirements for investments, and that they are not identical. She said that there are many different kinds of investments and that many of the reporting requirements are dependent upon the purpose of the investment – for example, whether it will be sold for a profit or held to maturity.

Mr. Allen said he thought that other than “held to maturity” all of the standard setters have pretty well gone with “fair value.” Ms. Parlow said that the FASB ED proposes that for certain investments, both amortized cost and fair value would be required to be presented and reconciled on the face of the balance sheet.

Mr. Allen said that the federal government’s investments are of a different nature than those in the private sector, where investments are made to make a profit. Ms. Parlow said that some of the federal government’s investments are for that purpose, also. Mr. Allen asked if “investments” are even the right category, for example, when the federal government is using resources to support the economy or an industry. He said that such actions could be called something like “interventions” or “economic stability outlays.” Ms. Parlow said that the difficult part is when the federal government receives some kind of an asset, in contrast to simply charging the outlay to expenses.

Mr. Allen said that when there's an action, there is an internal discussion of whether the action is a loan, an investment, or other asset. He said that this project should capture why the investment is being made. He said that in cases where the action is to promote economic stability, the standard should dictate how the accounting is done. He said that the accounting should be driven by the economic substance, and not by what we call something.

Mr. Dacey said that investments of federal entities that follow FASB, for example PBGC and TVA, are in a separate note. He said that the rest of the major investments relate to interventions, which are now valued at fair value, except for the loans, which are valued as credit reform loans, and FASAB already has a standard for credit reform loans. So, the question is, how much time do we want to spend developing a standard for something that we don't do very often, but we may do sometimes, and whether we think that the fair value model that is used now is an appropriate model going forward.

Ms. Kearney said she agrees that the scope of the project would be fairly narrow and that although she understands the complexity of the project, the time line goes out to a time when we might not even have those investments on our books. She asked if the Board really needs this project. She said that it might conserve resources if we base the project on what we're currently doing rather than doing in-depth research on the topic.

Mr. Dacey said that FASB's project is addressing a great deal of complexity that he is not sure is relevant for the federal government.

Mr. Steinberg said that if FASAB does not address this area, the hierarchy requires that entities go to FASB for guidance, and the FASB requirements are very complex. Mr. Dacey said that the hierarchy could go to "generally accepted practices," for which the federal government uses fair value.

Mr. Reger said that he believes that this project has a fairly significant priority, but agrees with Ms. Kearney that its scope should be narrowed. He said that it shouldn't be hard for FASAB to put out some guidance based on what's being done currently and have that out there until and unless other standard setters come up with something that seems to make more sense. He said that this project could be fairly simplistic and not spend a great deal of time doing research because the other standard setters' projects do not seem to be mature enough that we would end up with anything other than what we're doing currently. Mr. Showalter agreed.

Mr. Dacey said that although we are saying "fair value," there are different ways of deriving fair value, for example, for the Troubled Asset Relief Program (TARP) versus Fannie Mae and Freddie Mac. Mr. Showalter agreed.

Mr. Allen said that we do not need to re-invent the wheel - that we need to develop an inventory of what we have and how it's being valued, and perhaps it will be fairly simple to develop a standard. He said that the reason for the various loans and equity positions may be such that we need to do the same accounting for all of them to provide

the best picture of the economic value. He said that he found himself asking “why did we call this a loan? Why did we call this an equity investment?”

Mr. Dacey said that the assets take different legal forms, and does not anticipate this project evaluating alternative policy decisions that could have been made but were not. He said that virtually every TARP investment is based on discounted cash flows, except for those assets that have a current market, such as General Motors or AIG.

Ms. Parlow said that she is getting the impression that for bailout activities, which don't match the private sector business strategy at all, the Board would like to see a concept of fair value that would essentially codify what is being done now. She asked if SFFAS 2 is adequate for bailout activities and was adapted for bailout activities. Mr. Dacey said that, for the methodology used to value TARP investments, the only unique issue, based on the law, is that the discount rate is risk-adjusted, which is not prohibited by SFFAS 2.

Mr. Steinberg asked about re-estimates. Mr. Dacey said that re-estimates are done annually, based upon risk.

Mr. Granof asked how you can determine risk when you are addressing a sample of one. Mr. Dacey said that for example with banks, there is a process that evaluates risk. He said that he believes that the loan piece is fairly nominal at this point, and uses discounted estimated cash flows.

Ms. Parlow said that based on the Board's discussion, she could probably shorten the timeline quite a bit and shrink the task force down to just a few members, perhaps experts from the Treasury Department. Mr. Reger said that maybe it should also include someone from the GAO audit staff.

Mr. Dacey said that he would like to keep the project at a fairly high level and let the GAAP hierarchy pick up anything not addressed.

Ms. Kearny said that there should also be representation from OMB's credit reform experts; the other members concurred.

Mr. Allen recapped that this approach would allow the timeline of the project to be shortened.

**Conclusion:**

- The scope of the project will be narrowed to primarily address the federal government's bailout activities and will not include in-depth research of other standard setters.
- The task force will primarily include subject matter experts on the federal government's bailout activities and credit reform accounting from Treasury, GAO and OMB.

- Staff will revise the project timeline based upon the above changes.

- **Steering Committee Meeting**

The steering committee discussed the fiscal year 2012 budget and the small shortfall in Treasury's anticipated reimbursement. Ms. Payne committed to exploring ways to reduce administrative expenses in the coming year. Final decisions will be made once appropriations are finalized.

### **Adjournment**

The Board meeting adjourned for the day at 4:30 PM.

## ***Thursday, August 25, 2011***

### **Agenda Topics**

- **Asset Impairment**

Mr. Allen introduced the project by referring members to TAB I and asking Mr. Savini to begin the discussion.

Mr. Savini began the presentation by thanking those members who provided written comments prior to the meeting. Members all seemed to gravitate to the "limited and rare" language of the proposed standard located at paragraph 8, page 11 of the draft ED. Consistent with the task force's review, members have opined that if this language remains as-is, it will make the proposed standard in essence inoperable. In dealing with this problem, staff proposes that the Board adopt Mr. Showalter's suggested language. The suggested language follows:

The provisions of this standard are to be applied when indications of impairment, as specified in this standard, come to the attention of management, however that may occur. It is not the intent of the Board to require the agencies to conduct an annual or other periodic survey to identify such indications of impairment.

Mr. Jackson and Mr. Granof both concurred with Mr. Showalter's suggested language as they had similar concerns with paragraph 8.

Mr. Allen stated that although he agreed with the tone, he noted that impairments need to be significant and that the Board's standard should ask

entities to “keep their eyes high enough” to ensure that immaterial or insignificant matters are not reported. His concern is with Mr. Showalter’s suggested phrase, what “comes to the attention of management.”

Mr. Jackson noted that he also provided suggested language to Mr. Savini, However, he prefers Mr. Showalter’s language because in his proposed language he mentioned that entities would have systematic portfolio reviews and he was concerned that his own language might be interpreted as a Board requirement.

Mr. Schumacher referred members to paragraph 9 that defines impairment as being a significant decline in service and not normal or ordinary declines.

Mr. Savini noted that the auditors on the task force were similarly concerned that there should be a reasonable expectation that entities would have some type of internal control processes in place that would ensure reviews take place to periodically assess the adequacy of their assets. The auditors are sensitive to the fact that the draft ED might be interpreted as downplaying the importance of such internal controls or processes.

In response to the task force concerns, Mr. Dacey noted that he does not believe the Board is downplaying the importance of such internal controls or processes. He pointed out that by virtue of our deferred maintenance work alone; specifically SFFAS 40 and the current ED on measurement and reporting, the Board’s commitment to relevant internal controls or processes is self-evident. However, he wondered if there was a way we could link that work to this standard by indicating that deferred maintenance and repairs reporting is at least one source of information that could be used to assess significant impairment. As one reads the standard, it appears that a significant event must occur for an impairment to take place, however there should be systems in place that bring complete information to management on a regular basis.

Mr. Showalter concurred with Mr. Dacey stating that one of the elements of internal control is safeguarding assets.

Mr. Allen turned to staff and asked if this would be an appropriate topic for the basis for conclusions.

Staff replied in the affirmative stating that paragraph A10 on page 22 begins a basis for conclusions discussion entitled, “G-PP&E Impairments Can Also Be Identified from Asset Management Reviews.” Staff noted that this paragraph included three types of the more common PP&E assessments; condition, functionality, and obsolescence.

Mr. Dacey noted that he would prefer this discussion in the standard but does not feel too strongly about it either way.

Mr. Showalter then suggested that his phrase, “however that may occur”, could be footnoted or further elaborated in a manner consistent with paragraph A10 that would satisfy Mr. Dacey’s concern.

Mr. Dacey agreed with that suggestion.

However, Mr. Reger then asked if we even needed the phrase “however that may occur.” He noted that it would be sufficient to just state that the impairment indicators should come to the attention of management without adding “however that may occur.” Mr. Reger explained that this suggested phrase actually begs the question what does the Board mean by “however that may occur.” In essence what we are saying is that it doesn’t matter how it gets to management as long as it gets to them. He also noted that the phrase had an unintended interpretation or consequence that could lead one to assume that the Board had no expectations concerning internal controls or processes.

Mr. Showalter stated that when he added that phrase it was because he thought that impairment indicators can be brought to management’s attention by other than significant events or changes in circumstances. However, upon reflection Mr. Showalter agreed that if this language was achieving the opposite effect of its intention it could be deleted.

At this point Mr. Dacey stated that he would go even further by noting that if employees notice impairment indicators and are not communicating this upward, they need to be. However, he is not sure how the Board would put this into a standard. However, he does not want to go too far and say that there must be a structured process in place.

Mr. Allen then asked Ms. Payne if we could reference the standard to this portion of the basis for conclusions?

Ms. Payne replied that with the exception of illustrations, this is a practice most standard-setters try to avoid.

Mr. Dacey noted that the auditing standards have moved away from referencing to non-authoritative sources.

Mr. Jackson then noted that it would be just as easy to simply make the statement within the standard.

However, in so doing Mr. Allen noted that it becomes a defacto requirement; a should or must situation.

Replying to Mr. Allen, Mr. Jackson noted that he believes that referencing the standard to the basis for conclusions amounts to also creating a defacto requirement.

Mr. Allen then asked members if they would agree to including the word “significant” when referring to impairments.

Mr. Jackson noted that in the definition of impairment in paragraph 9, we already define the decline in service utility as being significant in nature and as such, there really would not be a need to have to add “significant” to the paragraph 8 language. The paragraph 8 language should include context. That is, some type of process that identifies impairments. For example, a sentence could be added such as, “a portfolio review may include periodic reviews of continual operational capability of PP&E or to assess deferred maintenance.” In this way, the Board sets up context of a review but it can be done concurrently with the requirements of meeting, for example, the deferred maintenance standard.

Mr. Dacey suggested that another way the Board could deal with this issue would be to add within the standard the lead-in language from paragraph A10; “Common indicators of potential impairment can be discovered during different types of asset management reviews...”

Mr. Jackson concurred with Mr. Dacey and noted that we need a sentence to create the expectation that something will happen {due to a process} as opposed to inferring that all a manager has to do is walk through a building and hope that an impairment indicator arises.

Mr. Dacey noted a concern with Mr. Showalter’s suggested phrase, “come to the attention of management.” He proposed that it should be replaced by “identified by the entity.” In this way, we focus on the entire entity, to include its internal controls and processes and not just “who it is.”

Noting an inconsistency, Mr. Reger then asked Mr. Jackson to clarify his position because the Mr. Showalter’s suggested language for paragraph 8 states that we do not require entities to do a periodic survey. However, his suggested sentence references periodic reviews. Are we implying that entities need to do a portfolio review?

Mr. Jackson agreed with Mr. Reger’s point and noted that in paragraph 8 he would include the word “solely” so that the sentence would read, “It is not the intention of the Board to require agencies to conduct an annual or other periodic survey SOLELY to identify such indications of impairment.” We do not want to require a portfolio review, however, the detection of impairments would occur coincident to other reviews an entity needs to comply with. We want to avoid having agencies set-up entire new processes for this standard. We need to link the identification of impairment indicators to processes they already have in



place. We need to remind them to keep the provisions of this impairment standard in mind when they execute requirements in other standards.

Mr. Reger suggested that we then take out references where we say we do not require reviews because it causes confusion.

Mr. Allen replied that he supports Mr. Reger's suggestion because it appears that the more members discuss this matter the more the expectation seems to be that we do in fact require such reviews. He suggested that we work with the language in paragraph 13 and then tie paragraphs eight, nine, and thirteen all together.

Ms. Kearney stated that she preferred the "It is not the intent" language because it is clear to the preparer. Also, she believes that the basis for conclusions would be appropriate to be elaborate and explain what the Board's opinions are regarding this matter.

In response to Ms. Kearney, Mr. Allen replied that he preferred leaving paragraph 13 in place as it is written because it is clear that "Absent any such events or changes in circumstances, entities are not required to perform additional procedures."

However, Mr. Steinberg responded that if the Board intended relying on paragraph 13, it might be best to strike the phrase "Absent any such events or changes in circumstances..." because this phrase qualifies or limits the fact that an entity is not to perform additional procedures.

Mr. Dacey noted that he had a contrary position because he doesn't know what we mean by the term "additional procedures"; additional to what? We are expecting entities to have a process that accumulates information as they perform concurrent reviews. It seems to be clearer in paragraph 8 than it does in paragraph 13.

Rounding out this portion of the discussion, Mr. Allen suggested that staff should continue work on the language ensuring that there are no inconsistencies.

One final point came from Ms. Kearney who suggested additional language at paragraph 8, line 10, at the end of the sentence to insert "remaining in use." By making this edit, it is clear to users that we are not discussing impairment of assets which are taken out of service and we achieve consistency with the introductory portion of the standard.

At this point, staff asked members to turn to page 28 to begin reviewing the draft flowchart. Staff specifically asked members if the process flow chart

generally reflected the Board's intentions. Staff then briefly reviewed each of the decision points and asked members for comment.

Mr. Allen stated that he liked the flowchart but that at the appropriate time, he wanted to discuss what constitutes "permanent" as we've described it at paragraph 16b.

Concerning the flowchart, Mr. Dacey inquired about the first decision point regarding the issue of whether a prominent or significant event or changed circumstances occur. He asked members if it was necessary to identify an event before an indicator. In many instances, indicators are the first things that are brought to senior management's attention.

Staff explained that the rationale for separating the event from the indicator is in essence to "filter" through and identify those impairments that are truly prominent or significant. For example, the terrorist attacks on September 11, 2001. It was obvious that they were indicators of impairment (e.g., physical damage) however, the most important thing that jumped out was the event itself. We are trying to separate the more ordinary and normal events from those that are different and unusual for the specific industry or environment that the entity operates in. In essence, it is hard to say that indicators or events should proceed one another since in fact, they can go either way.

Mr. Allen noted that many of the illustrations seem to be ordinary such as the mold example. How does this then relate to the first decision diamond?

Staff explained that the damage associated with an event does not give it prominence or significance, but rather the actual event is what drives whether the impairment is significant or prominent. For example, when the Pentagon was damaged one could argue that the type of damage was normal or ordinary but it was the event that gave the damage prominence. Another way of looking at this is that identical damage to a building can result from a hurricane or vandals; the difference is in the nature of the event.

Mr. Dacey replied that for that very reason he would recommend that the first two decision diamonds regarding events and indicators be treated as one.

Mr. Allen said he understands Mr. Dacey's point and acknowledges that significant events are key indicators. However, because the examples don't incorporate the significant event concept, the illustrated impairments would be excluded from reporting. For example, if an entire school or Smithsonian building is impacted, we need to be careful that we don't exclude these types of impairments because there is no significant event.

Staff stated that GASB 42 and our proposed illustrations pre-suppose that a significant or prominent event or changed circumstances occurred.

Mr. Dacey acknowledged the presupposition however, he went on to say that as currently illustrated, the flowchart would dismiss any potential impairment not brought about as a result of a significant or prominent event or changed circumstances.

Staff stated that the proposed standard is trying to address those impairments which should be reported and not necessarily addressing all impairments; e.g., those insignificant or non prominent type impairments. However, staff believes the flowchart addresses Mr. Dacey's concern because if the answer is "No" to whether or not a significant or prominent took place, we refer the preparer to the box which says that they consider adjusting depreciation methods, useful live, or salvage values.

Mr. Dacey stated that in order not to exclude those non-significant impairments he would prefer beginning with the identification of impairment indicators.

Concurring with Mr. Dacey, Mr. Jackson noted that because the condition might actually be identified before the event, he would maintain that both of these decision boxes be treated as one. For example, have one box that would simply read, "Are there indicators of impairment?"

Mr. Schumacher suggested the following, "has a permanent event occurred or are there other indicators of impairment."

Mr. Dacey and Mr. Allen agreed with Mr. Schumacher's language. Mr. Allen noted that you could add the term significant to impairment indicators; "has a permanent event occurred or are there other indicators of significant impairment?"

Mr. Jackson asked members if it would be best to simply begin with a question of whether or not an impairment indicator has been identified? You wouldn't have to say any more. Then as a follow-up question you would ask if the magnitude of the decline is significant.

Mr. Dacey expressed some concerns over Mr. Jackson's approach to focus solely on indicators.

Mr. Jackson replied by noting one would not even have to indicate significant within the flowchart. A question could be simply be, "has an impairment indicator been identified?"

Mr. Dacey stated that this week's earthquake was an event followed by an inspection of buildings for indicators. However, in other cases the indicator is known first before the event is identified. He clarified that he does not want to

change the concepts; but the ordering that could go either way depending upon the circumstances.

Mr. Allen summarized by saying that one could have a significant impairment without a significant event. He then asked members if they were agreeable to the Dacey/Jackson approach.

Members responded in the affirmative.

Staff then moved to the next decision diamond and paragraph 16a which discusses the magnitude of the decline in service utility. Staff stated that this is an area of managerial judgment. The task force reviewed this language in connection with illustration 4b on page 48 and determined it to be problematic. This language may make the impairment standard have no effect because management can determine that the service utility is reasonable in light of whatever it costs to maintain the asset in question. The task force advised that we delete illustration 4b. Staff and Board then reviewed and discussed illustration 4b in connection with paragraph 16a.

Mr. Jackson stated his concern was that on one hand in the bold titling we talk about the decline in service utility and then on the other hand in the narrative, we talk about the expenses of operation; an apparent inconsistency. He further noted that the title and the explanatory paragraph are not connected. The narrative language would need to change to reflect that the equipment or other property would continue to provide expected service utility for its intended purpose at the level for which it was intended to be used.

Both Mr. Allen and Mr. Jackson concurred that the titling should stand alone and not be changed.

Mr. Granof stated that he finds illustration 4b to be problematic in many ways. He noted that as written, we are relating current costs with future costs.

Mr. Jackson concurred with Mr. Allen's observation. He said he does not see this issue having anything to do with operating expenses. Staff raises a valid point by acknowledging that the explanation of the decline in service utility is not consistent with what persons would think the decline in service utility should be.

Mr. Steinberg stated that the illustration contradicts paragraph 16a. Using the facility for storage while maintaining it as a training facility would result in significantly higher costs than what one would want to pay for storage. In his opinion, the language in 16a is fine; it is the illustration that is problematic.

Mr. Granof agreed that the illustration should be deleted.

Staff also concurred that the illustration should be deleted.

Mr. Dacey asked a general question concerning illustrations 4a and 4b. He struggled with the application of operating costs in a decision regarding whether or not a change in manner or use of a facility should result in an asset impairment. In both illustrations, the asset continues to provide some level of service albeit different, such as training to storage. We might have to explain paragraph 16a in a technical bulletin or expand it here. In any event, we need to decide if we have decreased utility in an asset due to change in purpose that continues to be used whether we will have to take a write-down. And if so, why are operating costs a relevant factor to that decision? It seems that we will have to decide one way or the other whether to write the asset down and take a lower depreciation amount as a storage facility or keep depreciating at the existing book value.

Mr. Granof asked Mr. Dacey if the previous expenses which he considers to be sunk costs, are relevant?

Mr. Dacey replied by saying that one would have to determine what to do on the cost side.

Responding to Mr. Granof's question and Mr. Dacey's reply, Mr. Steinberg stated that this is what an asset impairment loss adjustment does; it reduces subsequent costs by lowering the basis and resultant depreciation.

Mr. Reger then asked if changing a training facility to a storage facility is in fact an impairment. For example, many agriculture department buildings are converted to barns or maintenance sheds. This is a frequent occurrence. The value and use of the building certainly change but it was not a result of a significant event. It was just the result of the course of a normal management function. That is, why is the normal life-cycle trend of a building's use an impairment situation?

In reply, Mr. Allen referred members to paragraph 10 that touches upon Mr. Reger's barn example by saying that different intended uses due to decreased utilization are excluded from impairment.

Mr. Reger said that paragraph 10 also read that way to him however, in looking at the illustration he was unsure if the change to a storage facility was a result of the inability of the training facility to continue being used as such or if it was a result of a management decision to make the conversion. In either way, it does not appear to be an impairment.

Mr. Granof disagreed by stating that he believed it was in fact an impairment. If the building is expected to provide a certain level of service and all of a sudden you're going to use it for a different reason such a storage, that is an impairment. If for example, a building that is carried at a million dollars and all of

a sudden it's converted to a barn worth \$200,000, that is most certainly an impairment.

Mr. Reger said that if there was still a need for training he would agree with Mr. Granof. However, if there was no longer such a need and if this could be considered a normal part of the building's life or operations there should not be an impairment recognition.

Mr. Jackson asked Mr. Granof to explain why an impairment loss would need to be recognized if management made a decision to use the investment in the training facility as continued use for storage?

Mr. Granof replied by saying that as a training facility there were certain inherent costs (e.g., windows, academic accoutrements, etc.) within the net book value of the asset that will be mis-matched against the future storage benefits.

Mr. Dacey said that it was a matter of timing as to when one would want to recognize those inherent costs or expenses of conversion.

Mr. Granof replied to Mr. Dacey's question by stating that the expenses should be recognized when, and in the period management makes the decision to make the change.

Mr. Allen, in concurring with Mr. Granof noted that the impairment principle is based on properly recognizing costs of service. This was the principal, at least at GASB that was followed. An entity would not be recognizing the correct costs of services by depreciating a building that was once a training facility and matching those costs to the storage facility. This cost of service implication occurs at the moment management makes the decision to change the use of the building from training to storage.

Mr. Granof stated that the impairment loss and book value write-down is made when management makes the change.

Ms. Kearney asked how frequently would this happen? If this happens frequently, are we not placing a significant burden upon the agencies? From an asset management perspective, costs of services or an asset's net book value might not be an asset management concern.

Mr. Allen replied by saying that materiality is the "huge saver." For example, is a barn at the department of agriculture going to be material to that entity's financial statements? The answer is obviously no.

Mr. Reger in referring to his earlier comments said that whether or not an impairment exists depends upon the ability of the building to fulfill its training

mission as opposed to management's intent. For example, take a college campus that has classrooms and a resultant change in programs leads to management to change the classrooms into something else; should this be an impairment? It should only be an impairment if it can no longer be used as a classroom facility not if management decides to change it to something else.

Mr. Allen disagreed with Mr. Reger.

Ms. Kearney made the distinction in Mr. Reger's argument that management was driven to change the use of the facility in one case whereas in the other it was a choice.

Mr. Reger agreed with Ms. Kearney's distinction by saying that in the case where management was driven to make the change an impairment should in fact be recognized. However, recalling the discussion earlier in the morning, Mr. Reger stated that he believes for impairment to exist there should be some type of event present that causes management to make the change in use. A management decision to use that building for something else should not be an impairment.

Mr. Allen replied that in the case of a change in demographics that occurs over time, such as a decline in the number of students, that condition is not tied to a specific event. However, the net result is still significant in that the school is now vacant.

Staff then noted that if there is no presupposition that a significant event occurred, Ms. Kearney's concern is that agencies will then drive the proposed standard down to a low level such as the barn example previously discussed. The task force also struggled with this balance of trying to keep management's eyes elevated and at the same time maintaining the relevance of the standard. Staff recommends that we make clear in the standard that we're looking for reportable impairments, that is, big ticket items and not necessarily what we need to account for. Asset impairments happen every day and depending upon the mission of the agency they are all different and as a result, agencies should be allowed to exercise their internal accounting policies in dealing with these issues via changes to depreciation methods, useful life estimates, etc.. We should make clear that we're not interested in these other types of impairments, but rather, those which are truly significant should be reported.

Ms. Kearney concurred with staff noting that she believes such clarification would address her concern. It would be impractical to ask agencies to apply this in a manner that would create increased burden and reporting volatility where an asset might be impaired in one year and then restored in another year due to management's decision to use the assets differently. However, if there is something not usual or ordinary to the agency driving that decision, she believes that under those circumstances the assets should be treated differently and made subject to this proposed standard. For example, if changes in

demographics forces an agency to change the use of the building then that could be considered something different. However, if management has a shortage of storage space and decides to temporarily use a school for storage she does not believe that the school should be subject to impairment.

Mr. Granof disagreed noting that the standard cannot be restricted just to “big ticket items.” The question is if the event is material. If so then you have to write the asset down.

Staff then challenged that notion by asking Mr. Granof if that is not exactly what GASB 42 has in fact done.

Mr. Granof replied by saying he does not believe the standard uses the word material.

However, Mr. Allen then noted that GASB 42 does use the word significant.

Mr. Dacey noted that he believes that what we mean by “significant” can be amplified. He believes that value-in-use has unique circumstances and he is not sure that the expenses to maintaining an asset are relevant to an impairment decision. He recommends expanding or clarifying paragraph 16a or it will be a source of confusion.

Mr. Granof concurred.

Staff then asked members if the concept in paragraph 16a of correlating/comparing expenses to expected service utility should be avoided. That is, does the Board believe we should do away with a quantitative concept and replace it with a qualitative concept?

Mr. Reger rephrased the staff position as either using the cost difference as a criteria or not.

Mr. Allen stated that he would do away with the entire concept/discussion. However, the cost difference is a criterion inasmuch as we’re attempting to get an accurate cost of services amount. This should not be limited just to a balance sheet perspective. We’re also looking at trying to measure the right amount for the operating statement. However, when seeing this illustrated in example 4b it raises questions.

Staff then noted that the issue of excess capacity for operational leverage needs to be considered by management. An entity may decide that it needs to retain that excess capacity or leverage. For example, regardless of operating costs it may one day take that school and revert it back from being a storage facility. In this case, as Ms. Kearney points out, it would not seem prudent to



take an impairment loss; in other words the magnitude of the service decline is not significant.

Mr. Dacey replied that when reading 16a, depreciation stands out as the main focus. For example, if \$100,000.00 of depreciation is being allocated to a storage facility where it should be \$10,000.00, then that difference is significant. The difference is what he believes is significant. As currently written, illustration 4b has to do more with management's judgment as opposed to an identification of a cost difference. If we can clarify 16a, it will achieve its intended purpose. Specifically, illustration 4b uses more subjective factors than the more objective factors referred to in 16a. If depreciation expense is going to materially change, then there should be an impairment adjustment because that would be deemed significant and to otherwise depreciate the higher net book value to the assets revised usage would be inappropriate resulting in overcharging costs. Mr. Dacey believes that if we clarify the paragraph and focus on depreciation which seems to be the driver of the decision, we would achieve our intent; greater accuracy in cost of services.

Mr. Granof noted that depreciation is a sunk cost and irrelevant to the decision.

Staff replied that paragraph 16a is not about comparing alternatives or options and as a result, depreciation is relevant and cannot be considered a sunk cost because we are attempting to compare costs of providing a service to the benefits received.

In reply to Mr. Granof, Mr. Allen concurred with Messrs. Savini and Dacey.

Mr. Granof disagreed noting that cost allocation of depreciation is irrelevant.

Mr. Jackson noted that there is a difference of opinion regarding depreciation and its related cost difference and how it may or may not be relevant. However, the central question is what criteria should one consider when ascertaining what a significant decline in service utility is. If the new "value in use" amount is significantly less than the existing structure's basis then that's an indicator; or if there is a massive drop in the depreciation amount that is also an indicator that something must be impaired.

Mr. Allen replied by noting that there could be different criteria depending upon the circumstances. For example, it might be a physical event such as the mold, or change in technology.

Staff acknowledged that if we were going to pursue a criteria based paragraph 16a, it would still allow management to use their professional judgment. Are we also then saying that in addition to quantitative criteria we will also include qualitative criteria?

Mr. Dacey responded that if measuring impairments is a quantitative calculation it would seem logical that the magnitude issue would be quantitative as well. Mixing in qualitative factors might not be helpful in this regard.

Staff acknowledged Mr. Dacey's comments and thanked him for the clarification.

Staff then proceeded to page 29 and reviewed the remaining steps in estimating a potential impairment loss and ultimately deciding if it should be reported. A brief review of the decision table on page 30 was also conducted.

Messrs. Allen, Dacey, and Granof suggested that instead of having an off page connector that the reference to decision table B could be added to the process box; "Estimate potential impairment loss."

Mr. Granof asked if it was appropriate to include a decision diamond concerning materiality because that is a concept inherently understood. This could be setting a bad precedent by specifying that materiality is part of this standard and that in other standards where we are silent, materiality it is not a consideration.

Mr. Allen replied that although Mr. Granof was technically correct, he believed it was appropriate because it was a reminder that part of the process includes a materiality consideration and that if the answer is "No" then an entity may wish to consider adjusting its depreciation methods, useful life or salvage value.

Mr. Dacey concurred with Mr. Allen noting that as long as it is not in the standard and only in the flowchart. The flowchart is a tool for the user and references to materiality seem appropriate. One could argue that this is redundant however it will ensure that we help minimize the amount of immaterial adjustments made.

Mr. Jackson stated that he saw references to materiality in the standard that they would have to be deleted. However, the flowchart reference serves as a good reminder.

Staff concurred with Mr. Jackson's observation concerning the existence and deletion of materiality references within the standard.

Mr. Allen asked Mr. Granof if he wanted to vote-out the matter. Mr. Granof deferred to his colleagues who did not object to a flowchart reference to "materiality."

In discussing the decision table on page 30 staff noted that at the prior Board meeting, Mr. Showalter had brought up the possibility of other potential measurement methods being used that the Board might be unaware of. The task force was asked this very question and they were unable to identify other

measurement methods. They suggested that if the Board so desired, we could address this matter in the last row of the decision table by referencing “other methods as appropriate.”

Mr. Showalter reminded the Board that he did not want to eliminate the possibility of future improvements that might occur in this area. Another idea could be to just include a footnote that says any other method that is commercially viable could be used. The Board should avoid being boxed-in to methods that over time might be improved or changed.

Mr. Allen suggested “other methods may be appropriate” to ensure that management doesn’t see an open-ended use of estimation methods.

Mr. Showalter agreed, noting that he would specify that it should be an industry accepted method.

Mr. Jackson suggested “other industry-accepted methods.”

Mr. Showalter agreed with Mr. Jackson’s suggested language.

Mr. Dacey asked members to parallel language in paragraph 17; “some acceptable methods”, implying that there may be other methods.

Mr. Granof had a question concerning the replacement/restoration approaches. What is the conceptual basis in the standard for these methods when the lost service utility is not going to be replaced or restored? In other words, what is the basis for using a method other than taking a percentage of the net book value (share of the historical cost) of the asset that has been impaired?

Mr. Allen responded by saying that every approach is intended to do just that. These are methods of calculating the allocation of that historical cost.

Mr. Granof then asked about the relevance of the current market value of the replacement or restoration approaches.

Mr. Allen explained that the methods are used to calculate via an estimate a percentage which is then applied to the historical cost amount.

Mr. Dacey noted that he also shared similar concerns to Mr. Granof’s mainly with the replacement approach. It seems that using this approach, management could drive to a calculation quite different than if it had used something like the service units approach. We see this in one of the examples where two of the three floors have lost their service utility and in one case 2/3 would be an appropriate adjustment but in the replacement approach it was significantly less.

After a brief discussion concerning the illustrations, staff asked members if the basic question was why include these two approaches at all. Mr. Granof agreed that that was the question at hand.

Staff proceeded to advise the members that the task force member who made this recommendation is an appraiser that worked with GASB in developing GASB 42. He advised that in measuring lost service utility, current estimates can be used and in the case of multi-use heritage assets, the distinction needs to be made that lost service utility is not replaced like in a modern office building but rather it is being restored. He advised that in estimating this lost service utility there would be significant differences in the amount of impairment loss calculated if either one of these methods were inter-changed or not used in connection with the appropriate nature of the asset.

Messrs. Dacey and Granof noted that they were concerned that either of these methods could result in over or under estimation of an impairment loss as compared to the other methods. This over or under estimation would depend upon the resultant estimates that were used in the calculation. The question is what is the relevance of using these current cost approaches to the historical values in question?

Staff explained that the conceptual basis is an imputed relationship of the current costs to either replace or restore the loss service utility, expressed as a percentage applied to the historical booked values.

Mr. Granof referred to illustration 1c logic and noted that following that logic in the example where we experience an impairment of five floors of a five story building, the resultant amount comes out to 97 percent and not 100 percent. Mr. Granof illustrated his point by a taking the wall remediation cost of \$2.4 million and dividing it by 40 percent which is the percentage of the total \$4 million mold remediation cost to yield a \$6 million estimate. This estimate represents what it would cost to remediate all floors. He then compared this \$6 million estimate with the PRV estimate of \$6.2 million to demonstrate that following the replacement approach one would impair only 97% (\$6 million divided by the \$6.2 million) and not 100% or all 5 floors.

Messrs. Dacey and Savini referred Mr. Granof to Illustration 1d and a brief discussion concerning the differences between these two illustrations ensued.

Mr. Jackson noted illustration 1d made the most sense because two of the five floors are 40 percent impaired and should be written off.

Staff noted that these two illustrations show that an entity could choose among methods. Illustration 1c uses the replacement approach and 1d uses service units approach. Staff went on to say that these are estimates and that any of

these figures could be interpreted in a manner that might not follow a linear calculation or concept and that in reality, if we knew all 5 floors were impaired, there would be no need for any calculation. Furthermore, all other standard setters use these methods in their illustrations. We are giving management different approaches to consider and they would be exercising the kind of judgment and analysis that we are doing at the table today.

Mr. Granof acknowledged that other standard-setters use these methods but in their illustrations they assume that the lost service utility will be restored.

Members continued to discuss the conceptual basis for using these two approaches when it is management's intent not to restore service utility. Staff referred members back to illustration 1c and noted that management will often obtain quotes or estimates regarding how much it would cost to fix or restore lost service utility prior to making an impairment decision. As such, these estimates would be readily available to be used to estimate the loss service utility. In other cases where management knows that it will not restore the service utility and as a result does not obtain quotes, they can use the service units approach as we show in illustration 1d. It is staff's opinion that in the end either method is acceptable because it provides for a reasonable estimate.

Mr. Allen concurred with staff noting that although there may be some merit in the conceptual application, we are dealing with estimates that require managerial judgment.

Messrs. Granof, Dacey, and Showalter continued having doubt concerning the application of these two methods.

Ms. Payne referred members to paragraph 17 that discusses using the measurement method that reasonably reflects to the diminished service utility. Is the intent is to measure the loss (lost service utility) or a portion of the historical cost of the net book value? If we're looking for the net book value adjustment then it would seem that we would need greater precision. However, if we're looking to estimate a loss it would seem that any of these methods could be used to reasonably estimate that amount. If it is precision in the net book value amount that we would like to achieve then she would suggest not using either the replacement or restoration approaches.

Mr. Jackson noted that the replacement approach could be skewed or tampered with.

Mr. Dacey stated that he believes the lost service utility (net book value adjustment) is what should be measured.

Ms. Payne suggested that staff review the conceptual underpinnings to these two approaches and consider how they may or may not relate to historical cost

(measuring loss service utility). A decision could be made as to whether to retain these approaches depending upon that research.

Mr. Reger stated that an alternative could be to combine the two approaches.

Mr. Allen asked staff not to drop the two methods but to research and make a recommendation to the Board.

Mr. Granof asked about the use of the undiscounted cash flow approach. What is the conceptual basis for using undiscounted cash flows?

Mr. Allen stated that for short-term periods the undiscounted cash flow approach is fine.

Mr. Dacey stated that he was fine with the methodology because we are trying to estimate if there is sufficient cash receipts to offset the depreciation costs (remaining net book value). In other words, we're trying to determine if the depreciation costs will have an equivalent amount of cash flows to be offset against.

Mr. Granof stated that there's no conceptual basis for saying that a dollar today is the same as a dollar to be received 100 years from now.

Members discussed the theory behind undiscounted and discounted cash flows in the context of inflation and purchasing power parity.

Reverting back to Mr. Granof's original question concerning the undiscounted cash flow approach, staff explained that the first test of recoverability is to use undiscounted cash flow. Once a determination is made that an asset might be potentially impaired, absent a net realizable value estimate as is the case in this illustration, we need to present value the undiscounted cash flow in order to determine the value-in-use estimate.

Mr. Jackson then addressed an additional point in illustration 7d on page 62. The title of the illustration is undiscounted cash flow approach however in the evaluation and measurement portions of the illustration we're using a discounted or present value approach.

Mr. Dacey responded to Mr. Jackson's observation by stating that he too was initially confused between this illustration and illustration 7c. However, the discounting or present value is a proxy for the value in use. The recoverability test in illustrations 7c and 7d use undiscounted cash flows, whereas the proxy for value-in-use in illustration 7d discounts or present values the undiscounted cash flows.

Mr. Granof asked if there was a slight inconsistency.

Mr. Dacey said the title should be clarified. He suggested making the title clearer for illustration 7d that the discounted cash flow is a proxy for the value in use.

Regarding this method, Mr. Reger and Mr. Jackson noted that the table in regards to this approach doesn't show events as do the other approaches and that staff should consider revising the potential indicators.

Staff concurred with the members' observation.

Mr. Jackson reminded the Board that illustrations need to explain and show the users how these approaches could be put into practice and that the Board should not necessarily favor any one approach over the other. Mr. Jackson is concerned that the table might infer a preference.

Messrs. Dacey and Jackson stated that they found the illustrations very helpful.

Staff noted that the reason the approaches were put into a tabular form and not a flowchart was in order to not suggest any preference. For example, if we had used a flowchart we would have directed people to a certain approach whereas the tabular format is seen as being less prescriptive.

Mr. Dacey suggested in that in the caption heading for potential indicators that a footnote be included that explains that these are for illustrative situations that might be appropriate given the circumstances.

Mr. Showalter stated that he saw no problem with the table because it was in the same order as the paragraph in the standard that lists the approaches.

Mr. Allen then directed members to paragraph 16b noting that the entire standard hinges on the issue of what is a permanent decline in service utility. What does this mean in an environment where budget resources/allocations are determining factors? For example, could one postpone the recognition of impairment for twenty years because they have hope that the budget appropriation would be forthcoming some day? The language that says "management has no reasonable expectation that the lost service utility will be replaced or restored" seems challenging. Should we define this closer by including for example, having specific plans to replace the lost service utility or that an entity is setting aside funding or that it has a history of restoring lost service utility in similar cases? Absent such criteria, hope springs eternal and this language would abrogate the reporting of any potential impairments. Does the Board want to drive this harder by saying that the impairment needs to first be measured and then absent any criteria to restore the loss service utility the loss would need to be reported?

Mr. Dacey noted that the decision needs to be very facts and circumstances based so the standard needs to be fairly principled while also being flexible. We might want to explain what we mean by reasonable expectation. We could add that even if management desires to restore the lost service utility, if the reality is that budget monies will not be available an impairment loss should be recognized.

Mr. Showalter stated that Mr. Allen's example of the twenty year expectation or hope would certainly not be considered reasonable. He believes that as Mr. Allen suggested, we should link reasonable expectations back to plans.

Mr. Steinberg asked members to refer to paragraph 11 where he highlighted the phrase "material impact to the financial statements." In most cases, any impairment would get lost because agencies have very high materiality thresholds due to their size. For example, an agency's headquarters building could be impaired and yet not have a material impact to the entity's financial statements. Is this paragraph as currently written going to rule out any recognition of impairment?

Mr. Allen noted that at the government-wide level he could not foresee any impairment being reported.

Mr. Dacey replied that the reality is that impairments will be recognized at the component level.

Mr. Steinberg reiterated that even the component level concerns him because of the immense size of agency balance sheets. In DOD's case one could close two or three entire bases and that would be immaterial.

Mr. Jackson replied by saying he could envision this in some type of the BRAC-like process where an entire piece or large portion of a portfolio are affected. This is another reason why we should not require a systematic process to identify impairments because in the end, they would probably all be immaterial. Additionally, this will probably only be applied by capital intensive agencies such as DOD, Interior, and Agriculture.

Mr. Dacey concurred with Mr. Steinberg, but noted that materiality provisions and considerations are part of any accounting standard.

Mr. Steinberg noted that the Board will be issuing a well written and well thought out standard that will probably not be used because of this paragraph 11 language.

Ms. Kearney replied that even if the language were deleted from this paragraph, the materiality provisions still apply and the result would be no different.



Mr. Jackson recalled that historically auditors were using the FASB impairment standard to review the agency assertions which in turn caused agencies to go through extensive review processes to comply with the auditor requests. Notwithstanding SFFAS 10, there was an absence in FASAB literature concerning impairment accounting. The auditing firms brought this to our attention. It was clear that we have a missing link in our PP&E literature. It became an emerging issue because the auditors were pushing the envelope understandably so. What we've done here is to outline a process and in the end, an agency would need to discuss materiality with its auditor. This proposed standard actually gives the agency a process to follow without requiring them to physically engage assets such as surveying their portfolios; which is something that the auditors were in essence requiring them to do.

Mr. Steinberg noted that Mr. Jackson's last point was a good reason for issuing the standard.

The last matter discussed was the applicability of this proposed standard to internal use software. The Board asked staff to do additional research in this area and develop a recommendation.

The Chairman concluded this portion of the meeting by thanking staff and members and asked that any other comments or suggestions should be provided to staff.

**Conclusion:** Staff will make the agreed edits and research the measurement methods further. The Board will receive a revised draft for consideration at the October meeting.

- **Removal from Service**

There were no objections from Board members to the issuance of Technical Release 14, *Implementation Guidance on the Accounting for the Disposal of General Property, Plant, & Equipment*. The technical release will be issued as final sometime after October 1, 2011.

## **Adjournment**

The meeting adjourned at 10:40 AM.