

FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD
December 4-5, 2007
Room 7C13
441 G Street NW
Washington, DC 20548

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Tuesday, December 4, 2007

Administrative Matters

- **Attendance**

The following members were present throughout the meeting: Messrs. Dacey, Farrell, Jackson, Murphy, Patton, Reid, Schumacher, and Steinberg. Chairman Allen was not present on Tuesday, December 4th but was present on Wednesday, December 5th. During his absence, Mr. Farrell served as chairman. Mr. Werfel was present with the exception of an absence from 11:30 to 2:00 on Tuesday, December 4th. The executive director, Ms. Payne, and general counsel, Mr. Jacobson, were present throughout the meeting.

- **Approval of Minutes**

The minutes were approved electronically before the meeting.

- **Updates from Members**

Mr. Jacobson, FASAB General Counsel, announced his retirement. He will be retiring on January 3, 2008. He introduced the new FASAB general counsel, Abe Dymond , to the members. He assured the members that he enjoyed his tenure with the Board and that the Board will be in good hands with Mr. Dymond .

Mr. Werfel updated the Board regarding the results of the fiscal 2007 financial statement audits. Nineteen agencies received clean audit opinions by November 15th. He noted that material weaknesses are down. Thirteen agencies have clean opinions with no material weaknesses. This includes some large agencies such as Interior and Justice. This is especially notable given the changes in audit standards recently as well as the perception in the community that auditors are getting tougher. Overall, the trend is in the right direction. The process associated with audited financial statements is clearly a priority. Agency heads are making the results of the audit a high priority and are taking note of success and failure.

Mr. Steinberg asked whether the reports are changing in length; perhaps getting shorter. Mr. Werfel noted that the pilot might be expected to have that effect but the data is not in yet. The pilot requires that agencies produce a highlights report. In addition, agencies were encouraged to consider their audience and produce a highlights report that is easier to understand. Eleven agencies participated in the pilot. The financial report was due November 15th but the performance report will come out next year. OMB plans a public hearing on the results of the pilot. OMB will ask six or seven questions of people from organizations such as AGA, Mercatus, as well as FASAB or FASAB staff. The hearing is expected in late March or early April.

Mr. Jackson noted that professional journals continue to report that CFOs aren't finding the information in financial reports to be very useful. This continues to be reported annually based on a survey. It would be interesting to know whether OMB or Treasury could delve into whether management has changed because of the improved quality of information. He noted that more accurate receivables, inventory and property data would be expected to lead to better decision making. He believes someone should stress the improvements in management that have come about by virtue of more reliable information.

Mr. Werfel responded that his boss challenged him to explain in plain language what the reduction in material weaknesses means. The example he used is unliquidated obligations. He noted that agencies have many transactions going on and sometimes the money in the pipeline gets stalled. Auditors ask why the

money is stalled and ask why the money can not be pulled back and used for other purposes. He drew the comparison between these incomplete transactions and an individual having a drawer full of completed and signed checks that have not been mailed. The questions that arise are (1) are there unpaid bills accruing late fees and (2) are some of the checks unnecessary and the related account balance available for new checks to cover other priorities.

Mr. Werfel indicated that the journalists seemed to understand this basic cash management issue. However, Transportation lost its clean opinion last year due to a construction in process issue, corrected the problem this year, and he is unable to say what management improvements may result from the enhanced controls in that area. This is an area he believes needs to be explored because of the resources invested in improving controls in this area; perhaps the answer is that in some cases you may not be able to draw such a direct link between internal controls over financial reporting and management.

Mr. Jackson indicated that in some cases the controls may affect program performance information. For example, delaying movement from in process to in service may affect reported costs but you may not have other management consequences. It would be interesting to get studies on some critical areas – what are the benefits of more reliable information. He believes there is a need to refute some of the articles that suggest clean opinions on audited financial reports have little value. He expects that view to be challenged somewhere along the line.

Mr. Werfel noted the CFO Council working group addressing these questions has identified three fundamental purposes - transparency, internal controls, and decision usefulness. Clearly the audited financial reports drive internal controls. The question is does the current model drive the right internal controls; do those things have value added in terms of making government more effective. With respect to transparency, the focus is shifting to the pilots and an expectation that the CFR's transparency needs may be different from the agency level transparency needs. A greater question is whether the information generated by the process can be used. He has not heard it asserted that the financial reports themselves drive decisions. Is the proof of the financial reporting system also proof that the agencies can use the system to generate decision useful information from systems tied to the financial reporting system?

Mr. Steinberg noted that OMB had reported to Congress on the benefits of audited financial statements when the CFO Act was first implemented. At the IRS, it was discovered that accounts receivable were stated at \$ 110 billion but were really \$80 billion and all but \$20 billion were uncollectible. They reduced the number of collectors by thousands. OPM had revolving funds intended to be self supporting – they got out of both of those businesses when the audited financial statements showed that each was losing \$50 million a year. . He indicated that there were four such cases used in the report to Congress.

Mr. Werfel expressed interest in the FASAB discussions that were beginning regarding PP&E accounting. Controls over inventory, receivables, and loans are clearly important to support decision making. He noted that property was considered a high risk area. He finds it odd that agencies having no material weaknesses over financial reporting regarding PP&E have been identified as having high risks related to PP&E. He wondered how that could be and hopes that a fresh look at PP&E standards would help explain that result. He'd like to see a closer nexus between PP&E controls and management. He believes something is misfiring on PP&E that is not occurring in other areas.

Mr. Farrell expected that if one studied the area, you would find the benefits. However, he suggested we move on to other topics. He opened the discussion of clippings. He expressed interest in the enhanced use of leasing and expected that such creative financing would be found throughout the government.

Members discussed leases; noting:

- the IASB effort to revise the standards for leases
- the new arrangements where private entities own toll roads
- the IPSASB has a project on public-private partnerships
- the problem of assets with considerable deferred maintenance being returned to the government at the end of the contract
- the existence of long-term leases that have the look and feel of a long-term lease but they avoid the capital lease arrangements
- VA regional headquarters have been built but only leased for 2 years – the deal looks like a capital lease but qualifies as an operating lease
- Treasury financing is the cheapest possible financing but there are incentives that lead to these creative project financing arrangements
- OMB's guidance provides that expected occupancy of more than 15 years triggers treatment of a capital acquisition; consequently, they often see 14 year occupancy arrangements

Ms. Payne explained that there had been great interest in the lease project but that the Board had previously decided to wait until the IASB project evolved further. She indicated that staff would provide information on the status of the IASB project soon.

Mr. Reid noted that fair value was being used to hold managers accountable for assets. Fair value changes the focus from an individual detailed cost accounting effort to a holistic approach of looking at the value of the assets as a whole. Our focus is bottom up and leads to detailed questions such as how to account for replacement parts and improvements. Fair value may get us away from figuring out how much we paid for an individual bulkhead.

Mr. Farrell noted that we would be talking about measurement attributes later in the day. Mr. Reid believes the property area is a grey spot and it may be fruitful to discuss our objectives.

Mr. Dacey noted that there is a case regarding the ability to collect revenue from oil and gas leases in the Gulf of Mexico. Mr. Murphy explained that Interior had mistakenly omitted specific provisions from leases and tried to impose the provision. He indicated that the legislation actually did not allow the collections Interior was trying to make for the period of 1995 to 2000.

Mr. Dacey noted that the SEC had permitted foreign filers to rely on IFRS without reconciliation. The SEC is also seeking comments on a proposal to allow US filers to opt to use IFRS in their filings.

Agenda Topics

- **Communication Methods (Conceptual Framework)**

Overview

The primary objective for the December 2007 communication methods topic was to discuss a proposed concepts statement that would amend SFFAC 2, *Entity and Display*. During the Board's September 2007 meeting, members agreed that there are a number of factors to consider when determining how to communicate required information and those factors are presented in the basis for conclusions section of SFFAS 25, *Reclassification of Stewardship Responsibilities and Eliminating the Current Services Assessment* (Figure 2). Members relied on the factors when developing the standard and found them helpful for distinguishing basic information from required supplemental information (RSI). The Board agreed that a concepts statement on communication methods should include the SFFAS 25 factors.

Rather than developing a new concepts statement that would include the factors for distinguishing basic and RSI, staff proposed a concepts statement that would amend SFFAC 2. The existing FASAB conceptual framework currently includes some guidance for communication methods. For example, SFFAC 2 discusses types of financial statements, management's discussion and analysis, and RSI, and SFFAC 3, *Management's Discussion and Analysis* further discusses the MD&A. Amending SFFAC 2 to include the factors for distinguishing basic and RSI would help reduce the likelihood of repeating existing concepts in a new standard.

The Board agreed with the staff proposal to amend SFFAC 2 and provided comments on the content of the proposed statement. Staff plans to prepare a ballot draft for the February 2008 Board meeting. Accordingly, staff intends to revise the statement and address any additional Board comments prior to the February 2008 Board meeting.

In addition, staff noted that discussing required information categories raises another matter for the Board's consideration. Staff noted that the Required Supplementary Stewardship Information (RSSI) category remains a part of the federal financial reporting model. The Board has reclassified all RSSI items except Stewardship Investments. Stewardship Investments include investments in non-federal physical property, research and development, and human capital. Members noted that the information is currently being treated as RSI; however, when the Board originally created the category, the Board expected that the auditor would report on this information in a manner similar to basic information. Also, some members expressed concern whether the information should continue to be required.

The Board agreed to consider a project on the RSSI category during its February 2008 technical agenda setting discussions. Additional details of the discussion are as follows.

Discussion

Members sought clarification on whether there would be a difference in the due process steps for an amendment versus developing a new concepts statement. Ms. Payne explained that the due process would be the same.

Mr. Werfel explained that from a practical standpoint, the Board could use the factors to help choose between basic and RSI when developing a standard. He noted that the factors are rather intuitive and he suggested that the Board not spend significant resources editing or deliberating them.

Ms. Payne stated that to reduce the possibility of spending resources on editorial issues, staff plans to suggest additional amendments to SFFAC 2 in stages. Staff noted that an amendment may be needed to update some of the SFFAC 2 guidance, such as changing General Accounting Office to Government Accountability Office (GAO), while other amendments are a part of on-going Board projects, such as the projects on Social Insurance and Fiscal Sustainability. Staff may propose additional amendments as these projects further develop.

Mr. Farrell noted that the verb tense or modifier in some of the factors may confuse a reader, such as the factor, "Preparers' discretion in preparing and presenting the information." In theory, the preparer does not have discretion in presenting the information, its how the information is presented.

Mr. Jackson added that the factor noted by Mr. Farrell and the factor, "Strength of signal Board wishes to be sent in the financial report," are not meaningful. The factor, "Significance, relevance, or importance of the item in light of Objectives," is important. Mr. Reid noted that the strength of signal factor relates to the level of effort required when information is subject to audit scrutiny. Members agreed that the factors are intuitive and changes should be minimal.

Mr. Werfel stated that this year, the Office of Management and Budget moved the Statement of Financing from the financial statements to disclosure in the notes. The financial reporting community believed that the statement is a reconciliation exercise rather than a statement. Going forward, the community would like to move the statement to RSI. Mr. Werfel asked whether the proposed amendment to SFFAC 2 would need to be finalized before the Board decides on the placement of the statement of financing. Ms. Payne stated that SFFAS 7 addressed the placement of the statement of financing and the topic would be a separate project. She noted that the statement of financing topic could be raised during the technical agenda setting session in February 2008.

Ms. Payne noted that in order to make progress on the proposed amendment to SFFAC 2, staff plans to provide the Board with revised drafts between now and the February 2008 Board meeting. For the February 2008 meeting, staff will provide members with a ballot draft in their binders. If no issues need to be raised, the proposal would not be on the agenda for discussion.

Mr. Steinberg stated that FASAB sets GAAP and defines the financial statements, notes, and RSI that should be reported. Agencies publish the financial statements, notes, and RSI to demonstrate accountability. In many ways, OMB decides what the agencies should report and OMB does state the financial statements that should be reported. However, the financial statements are only a part of what OMB requires. The OMB feels that there are items necessary to demonstrate accountability that go beyond financial statements. Mr. Steinberg expressed concern whether SFFACs 1 and 2 addresses this notion. He also noted that the agencies believe that accountability reports include general purpose financial statements.

Ms. Payne stated that SFFACs 1 and 2 acknowledges the breadth of information needed in a general purpose federal financial report (GPFFR). The term GPFFR is not intended to exclude non-financial information. SFFACs 1 and 2 discuss performance information and information on systems and control. The conceptual framework acknowledges the necessity of integrating various items of information. However, the current proposed amendment to SFFAC 2 focuses on the assurance categories and amendments relating to the reporting model will follow. The reporting model phase can serve as a vehicle to integrate the whole effort, such as OMB's requirements and GAO's internal control standards, and better explain the necessity to integrate the efforts and the GAAP portion within that integrated framework.

Ms. Payne noted that at the staff has considered an accountability report and GPFFR as one and the same.

Mr. Dacey noted that there are two factors that focus on the balance sheet and statement of changes and may need to be broadened to address other considerations that FASAB has such as the statement of social insurance. Those factors are "Use of historical financial data or financial transaction data"

and “Relevance to measuring financial position or changes in financial position.” Mr. Jackson added that information like that which would be in a statement of sustainability or social insurance requires projections and looks into the future. One may not want to stay with the mindset of looking historically.

Staff noted that the Table of factors reflects different views of financial statements. Some factors, like the factor regarding financial transaction data, reflect a traditional view while a factor like the importance of the information in light of the objectives reflects a broader view. The Table does not suggest one view over another.

Members provided the following additional comments on the proposed statement.

- Paragraph 73A. The first sentence discusses the auditor’s opinion. However, the auditor’s opinion should not be the primary focus for describing basic information. The paragraph should start with the second sentence.
- Paragraph 73D. The paragraph should include the notion that RSI may not be subject to reliable estimation. The Board may believe that an item of information is important to the fair presentation of the financial statements; however, if the item is not subject to reliable estimation it cannot be considered basic. In the past, the Board determined initially to consider deferred maintenance as basic information. The Board later reconsidered this decision and moved deferred maintenance to RSI because the information was not subject to reliable and consistent estimation. In addition, the Board may want to assess new information before considering it as basic and subjecting the information to audit. For instance, social insurance was considered stewardship information, which was treated as RSI, prior to being considered basic.
- Paragraph 73E. Involves multiple topics that could be better discussed as separate paragraphs or simply deleted because it includes a discussion of a factor as an example for distinguishing RSI from Basic. Discussing a particular factor may cause some users to view one factor as more important than others. As an alternative, to help a reader better understand a factor, a footnote could be added to the Table of factors. The footnote could provide an explanation of the factor.
- Paragraph 73F. The paragraph appears to repeat a discussion stated earlier in the document (paragraph 55B).
- Footnote 11 may no longer be pertinent.

Ms. Payne noted that she has been reviewing the internal policies for staff and revising some of the boilerplate approach for exposure drafts. One change to the

boilerplate was reducing the number of questions in the Executive Summary from four to two. Although the questions had a different focus, they tended to overlap.

On behalf of Mr. Allen, Mr. Farrell noted that page 8 of the proposed concepts statement includes language that asks respondents to comment on the expected benefits and perceived costs of the statement. Mr. Farrell asked the Board to consider removing this request for proposed concepts statements. Unlike standards, concepts statements are not intended to drive accounting practice. The Board uses concepts statements to develop standards. Members agreed that the language was not appropriate for a concepts statement.

Mr. Schumacher noted that the staff discussion paper points out that RSSI remains a category for the Board's consideration. However, another category, Other Accompanying Information (OAI), is not discussed. Members noted that discussing OAI will bring all the information category terms to the forefront for Board consideration. This would reduce the need for the Board to consult the auditing literature for language often used in its deliberations. Staff noted that the focus of the proposed concepts statement was distinguishing "required" information, and OAI may be discussed in the existing concepts.¹ Members believed that the category should either be discussed or there should be an explanation of why the category is not discussed.

Regarding RSSI, members noted that the category was considered to be more than RSI, but less than basic. However, the category caused a lot of confusion in the financial reporting community and is currently treated as RSI. Stewardship investments remained in RSSI because it required a level of research which would have competed with other projects. At that time, some members wanted to reclassify the information to RSI while others did not believe the information should be required. Also, currently members question whether the information is useful. The information is not subject to audit. Members agreed to consider the RSSI topic as part of its technical agenda setting efforts in February 2008.

CONCLUSIONS: The Board agreed with the staff proposal to amend SFFAC 2 and provided comments on the content of the proposed statement. Staff plans to prepare a ballot draft for the February 2008 Board meeting. Accordingly, staff intends to revise the statement and address any additional Board comments prior to the February 2008 Board meeting. In addition, the Board agreed to consider a project on the RSSI category during its February 2008 technical agenda setting discussions.

¹ SFFAC 2, par. 54 discusses the notion of management communicating information voluntarily, but does not use the term OAI. The term OAI is used in SFFAC 3, Figure 1: Schematic Diagram of a Sample General Purpose Federal Financial Report.

- **Federal Entity**

Mr. Farrell explained that staff member Ms. Loughan would be unable to attend the Board meeting due to a medical situation. He explained that in previous Board meetings, the Board approved three general principles that would be relied upon in establishing the boundaries of the federal reporting entity. The broad principles are :

- the federal government is directly financially accountable for or owns;
- the federal government exercises control over; or
- the nature and significance of their relationships with the federal government are such that the exclusion would cause the government's financial statements to be misleading or incomplete.

The Board materials for the December meeting included the outline paper as well as an Appendix with reference materials presented at previous Board meetings. Staff continued developing the outline paper on the boundaries of the reporting entity and it includes specific, detailed criteria for each of the broad areas identified as well as an expanded introduction that includes a discussion of component reporting entities. Mr. Farrell noted that staff plans to move forward by forming a task force to share the outline paper for comment. The task force will include members from the CFO, OIG, and IPA as well as specific representatives from quasi government / hybrid organizations (such as FFRDCs), and intelligence agencies because of their unique nature. Mr. Farrell explained that the task force would be developing more specifics and examples for the paper. The task force would in essence serve as a technical panel to test criteria included in the outline paper.

Mr. Farrell explained that the goal for the meeting would be to discuss Board concerns on the direction of the paper. He stated that staff is not requesting the Board to discuss the specific language but instead to provide overall comments on the general principles. Staff would like the Board's concerns that should be addressed and incorporated into the paper prior to providing the paper to the task force.

Mr. Farrell directed the Board to page 6 of the paper that discussed the broad principles for the boundaries of the reporting entity. Mr. Farrell requested the Board's input on the three principles listed as this serves as the basis for the standard and the task force's work. Ms. Payne also explained that staff had developed an introduction section for the paper. She explained that the introduction discussed the relationship of the component reporting entities and the overall federal reporting entity. Ms. Payne explained that the paper states the general principles for defining the boundaries of the component reporting entities is the same as the principles for the federal reporting entity. Ms. Payne requested the Board's input and whether they agree the general principles are the same for both the federal reporting entity and the component reporting entity.

Mr. Steinberg explained that he believes control at the component level is very different than control at the government-wide level. He explained it is straight forward to see how the President and Congress exercises control but it would be much more difficult to assess the control of an agency head. Mr. Steinberg elaborated that the phrase “directing the financial and operating policies” is much easier to understand with the President when compared to that of an agency head.

Mr. Jacobson explained that the wording intentionally states that “all organizations within the three branches of the federal government” is part of the federal reporting entity. He explained that if it is part of the three branches, no further assessment is required. Organizations outside of the branches or whose legal status is outside of the federal government are the ones that would be assessed against the criteria. Mr. Jacobson suggested that certain aspects of the paper should be clarified to make this distinction.

Mr. Steinberg reiterated that assessing whether an agency controls another organization would be difficult. Ms. Payne suggested there are situations where control can be assessed at a component entity level. She explained an example with the SEC approving the budget and making appointments to the PCAOB. Ms. Payne noted that the outline paper discussion of control referred to the ‘federal government’ and indications of how it exercises control. Ms. Payne noted this should be clarified to explain that it is the federal government acting through a component entity and control can be assessed at a component entity level.

Mr. Farrell explained that in reading the paper he attempted to try to relate specific entity examples versus determining if these are the right concepts. For example, in the paper recently there was an article about Congress trying to intervene with banks on mortgage issues and one could say this is a form of control. Mr. Farrell explained the challenge is to address these types of situations conceptually versus assessing each organization to determine if it should be included in the federal entity.

Mr. Werfel agreed and stated that he was concerned with the use of the word “or” in the bullets with the general principles and suggested it should be “and” so that all conditions must be met. He explained that the federal government regulates almost everything (such as emissions) and that is a form of control. However, that doesn’t mean everything should be included. Mr. Murphy explained that certain issues should be addressed in the definition of control. He explained the federal government does control many things, but there is a point where it controls in a manner that would warrant inclusion in the federal entity. Mr. Murphy stated the use of a task force would be beneficial and would allow input for the development of the control definition. He explained control is the key element for inclusion in the federal entity. Mr. Murphy added the definition of control in the paper needs additional work. Mr. Werfel agreed but also suggested that “or” should be changed to “and” in the general principles because

he believes all three general principles are integrated with one another and should not be looked at separately.

Mr. Reid explained there a number of examples where the federal government exercises control over private enterprises that is subject to control of the government. Additionally, there are hundreds of organizations that are included in the budget, but they are totally self-sustaining and have no impact on the budget. He explained based on current practice these types of organizations are included in the federal entity.

Mr. Werfel asked what is meant by the phrase “financially accountable” in the first general principle. Ms. Payne explained that financially accountable is that an organization is in the budget and has a responsibility to report back to Congress on the budget. Mr. Reid explained it includes those organizations that we report the receipts or outlays. Mr. Reid explained the gray area often includes those organizations that are not fully funded by the federal government.

Mr. Jacobson explained staff included “or” in the general principles because there could be a situation presently or in the future where the federal government has complete control but is not financially accountable.

Mr. Reid explained there could be organizations that are controlled by the federal government and included in the budget; but if that organization should cease then all of the assets would go back to the owners or stockholders. He explained it would in essence be an outlay of the federal government. He also noted there are situations where the federal government may own all the assets because they were purchased with federal monies. Mr. Reid agreed with Mr. Werfel and the principles should be looked at together and the term “and” should be used.

Mr. Farrell explained that he believes “and” would be appropriate for certain situations while “or” would be appropriate for other situations. Mr. Werfel agreed and suggested perhaps the task force could address this issue. Mr. Werfel explained the example where a grantee purchases assets with federal funds and the federal government has an interest in those assets and does exercise some forms of control. However, he stated no one would believe the grantee should be consolidated with the federal entity. Mr. Werfel suggested the concept of control is very complicated.

Ms. Payne explained that the complexities with control have been long-standing. There have been several occasions in the past where workgroups have used the indicative criteria set forth in SFFAC 2 to determine if an organization should be included. She explained this project will build upon the criteria in SFFAC 2 and improve them as necessary to be included in a standard.

Mr. Jacobsen noted staff was careful not to make the definition of control all-inclusive. He noted that page 15 of the paper describes situations where control does not exist. He added the paper states that regulatory powers and purchase

powers are situations where control does not exist for purposes of including the organizations in the federal entity. He explained there is a big challenge in developing a definition for control that is not too broad or inadvertently too narrow so you include the appropriate organizations.

Mr. Farrell suggested that another area for consideration is the federal government's residual interest in assets as a result of a transaction. He noted that the government may have a residual interest in certain areas that may not lead to consolidation but would warrant some sort of accounting disclosure. Mr. Werfel explained that this has come up in practice as there are certain examples where Congress may state they want the organization to be able to keep the residuals if the assets are sold. Mr. Werfel also explained that he believes there would be measurement issues in calling such properties federal assets. Ms. Payne stated it was important to keep in mind this project is considering organizations for inclusion, not individual transactions or assets.

Mr. Jackson stated OMB guidance and SFFAS 6 addresses property in which the government has a reversionary interest and such property is not subject to inclusion. He explained that there are thousands of grantees that purchase assets with federal funds and they are not included in the federal entity.

Mr. Werfel stated he is interested in allowing the task force to address the "and" versus "or" issue, the definition of control, and performing an analysis of some of the practicality issues and what the impact is. He would like the task force to provide examples of how certain organizations such as FFRDCs or the Federal Reserve would be treated under the stated criteria for the Board's consideration.

Mr. Murphy explained often there are very similar things going on in the federal government but they are not accounted for similar in the budget. For example, there are several affordable housing programs in the federal government but some are on budget while others are off budget.

Ms. Payne explained there was an example with the Universal Service Fund at the FCC. She explained at the staff level, it was believed that it should be included after applying SFFAC 2 criteria. The Board noted that there are numerous examples that need to be evaluated against the criteria.

Mr. Steinberg explained that in the deliberations for SFFAC 2 it was agreed the Federal Reserve clearly met criteria to be included in the federal reporting entity. However, there was strong support to keep the central banking function separate and independent. Mr. Farrell indicated it is acceptable to include exceptions in a standard.

Mr. Steinberg stated that although ownership is included as indicative criteria in SFFAC 2, he finds it difficult to apply ownership. Mr. Jacobsen explained that the federal government has preferred stock in Amtrak and Chrysler. Mr. Murphy explained that there are situations when the government owns the stock of

criminals but there is no intention to keep it. Mr. Farrell explained that there are situations of temporary ownership. Mr. Steinberg stated that if we keep ownership then it should be clear that temporary ownership is excluded. Mr. Steinberg explained that he believes financially accountable is appropriate but the ownership needs to be looked at further. The Board agreed to have the task force assess whether ownership should be included.

Mr. Steinberg explained the third general principle related to completeness is problematic as it deals with judgment. He believes there needs to be specific criteria. Mr. Farrell suggested that instead of criteria, perhaps examples of situations would be more appropriate. Mr. Steinberg agreed that this might more appropriate.

Mr. Steinberg explained he believes the indicative criteria in SFFAC 2 have been able to handle most situations that have come up. He noted the only concerns have been with addressing FFRDCs, not for profits, and federally chartered organizations. He noted these areas were included in the last section on unique relationships in the outline paper. He asked whether the standard would take a position on each of these. Ms. Payne explained that the goal was to establish a standard that would be applied globally to situations. One of the basic premises in this project was to write a standard with guidelines and criteria but not to identify specific entities or state which entities should be in or out. Ms. Payne asked if the Board believes the standard should be written for the users to apply or should it be written to address specific types of organizations and direct specific results.

Mr. Steinberg stated he would prefer the standard explicitly state which types of organizations should be in and which would be excluded. He would prefer the proposal be included in an exposure for comment. He believes it should be handled in that manner or questions will continue to exist in applying criteria and uncertainty. Mr. Reid agreed with Mr. Steinberg and added that it would be preferred that the standard be definitive for consistency. Mr. Farrell suggested this would be more of a rules based versus principles based approach.

Ms. Payne explained that there are difficulties in a rules based approach because of differences in names/terminology and whether the substance is the same. For example, she is asked if an occupancy agreement is the same thing as a lease. Also, often relationships and agreements change among organizations that may affect the outcome. Ms. Payne stated that it is reasonable to include some concrete proposals in the exposure process. Mr. Steinberg explained that the difference in terminology can be addressed by clearly stating it is the substance of the relationship that matters.

Mr. Patton explained he has concerns with the definition and discussion of ownership in the paper. He noted the Board agreed to have the task force look at the definition. Mr. Patton also explained he was concerned with the definition of control. He noted that there has been long debate by the Board in the past

over active control or the ability to control. Mr. Patton asked if the document means active and current control. Ms. Payne stated yes and staff would ensure it was clear in the document.

Mr. Patton explained the third general principle (regarding organizations that if excluded would be misleading or incomplete) is too vague. He explained the need to add something to give it meaning rather than basing it on judgment. He suggested a solution would be that the underlying criteria for those situations be included in the criteria listing.

Mr. Patton explained the benefit criterion isn't mentioned explicitly. Ms. Payne explained staff included benefit in the definition of control as follows "control is the power to govern the financial and operating policies of another organization with expected benefits (or the risk of loss) to the reporting entity from the other organization's activities." She explained that staff included the language to specify that we weren't just looking at the ability to control, but the ability to control with these conditions.

Mr. Jackson asked if "benefits" means strictly a direct financial benefit. Ms. Payne explained that it is meant more broadly as the paper notes it may be a financial or non-financial benefit. For example, the federal government may benefit from a service being provided on its behalf.

Mr. Shumacher agreed with Mr. Patton's point regarding the third principle is too vague and there needs to be criteria for it. Mr. Shumacher stated page 5 of the paper addresses entities not reporting and he agrees that there are entities not reporting because they are not compelled to do so. However, he explained the paper states "although the entities may not issue their own stand-alone financial statements, the entities should provide the necessary information to ensure the larger reporting entity and ultimately the federal reporting entity are complete." Mr. Shumacher asked if the standard would address this further and how FASAB could require certain entities to report that are not required to do so. Ms. Payne explained that FASAB doesn't have the authority to require entities to report. She explained this is included to state what should be happening but it would not be included in the standards section.

Mr. Dacey mentioned that we discussed exclusions or things that would be misleading if excluded. He asked if there were examples of where it would be misleading if an organization is inappropriately included even if it meets some of the criteria.

Mr. Dacey explained there are certain organizations where it meets the criteria for inclusion but there is also another side of the organization that is privately funded and operated (such as the Smithsonian). He asked whether it would be appropriate to consolidate the entire organization or just the federal part.

Mr. Dacey also suggested there are organizations that may not meet the criteria for inclusion but there is a significant relationship such as related party and what disclosures would be appropriate.

Mr. Dacey also suggested that it would be a good idea for the task force to assess how proposals would affect existing practices. He questioned if it would cause a big shift in existing entities because consistency is important. He explained that it would not be beneficial to shift things tremendously and reporting entities in the process if it can be avoided. Ms. Payne explained the goal is completeness for the component reporting entities and the federal reporting entities. She explained this may be difficult because the component entities don't represent a complete economic entity individually. Mr. Dacey explained that creates an interesting situation for things that may be included in a component entity but not the federal entity.

Mr. Farrell suggested it may be beneficial to summarize the points for consideration by staff and the task force to ensure the Board agrees. He explained the main areas include:

- whether “is” or “and” should be used with the general principles, meaning do all conditions have to met for inclusion;
- further development of the definitions;
- developing examples of entities would be beneficial for the criteria;
- determining whether ownership should be included or if applicable in the federal government and if included, how temporary ownership should be addressed;
- further development of the third general principle as it is too vague— consider if specific criteria or examples or both should be included and also consider if there are inclusions (along with exclusions) that could be misleading and should also be addressed;
- should the standard be a broad based principles standard that can be applied or should it include specifics as to which type of entity should be included or excluded;
- further consideration of control versus ability to control which is discussed in the elements concept statement and ensure consistency in this document and that the meaning is clear;
- consider whether the word benefit in the control definition should be elaborated to discuss non-financial benefits and distinguish between financial and economic benefits;
- consider organizations that have both public and private aspects to them such as funding comes from both sources and how those should be treated, is it just the federal portion or is there some form of blending;
- consideration of other disclosures for organizations that are determined to be excluded from the federal reporting entity such as related parties; and
- there is concern over changing the whole organizational structure of the reporting entities as a result of this project so consideration should be given to current practices

Board members offered the following additional areas:

- Mr. Reid suggested that the project should address those entities not reporting that don't submit the required information. For example, the judicial branch does not submit the necessary information. Mr. Reid explained there are audit implications with this so how should it be addressed. Mr. Jackson explained that the dollars are nominal so it has not been pursued. Mr. Reid suggested perhaps some disclosure could be provided to say they are not included but this still is in conformance with GAAP.
- Mr. Steinberg suggested the task force should consider alternate display presentations and whether certain consolidated entities should be displayed on the face of the financial statement or footnote.

Mr. Patton explained it appeared the Board was expanding the scope of the project beyond consolidation. He explained this would be considered a major change. He added that he would reconsider his thinking on the general principles if the project was to include other types of disclosures versus strictly consolidation. He explained the criteria could be much looser if it were to address both. He suggested it may be more appropriate to have two sets of criteria—one for consolidation and another for including other disclosures.

Ms. Payne explained the project plan did include consideration of other disclosures for organizations that were not consolidated. Ms. Payne explained that she didn't see it as expanding the scope but instead expanding the options. Mr. Patton explained that his understanding was that "including" meant consolidating but if that also means disclosure then we may need to have two sets of criteria to address each. He added the general principles are not adequate to also address situations where other disclosures are required. Ms. Payne asked if it would be appropriate to explore the options before we get the criteria firm and come back with some examples of how to include without consolidating. She explained that could in essence drive the criteria. Mr. Patton suggested that it should be looked at simultaneously as it would be difficult to know the cut-off for consolidation without knowing the alternate ways of inclusion and what those criteria might be. Mr. Patton explained that he is not arguing against expanding the project, he just believes it would change the criteria if it is to also address including those organizations for disclosure versus consolidation.

Mr. Farrell agreed it does appear the Board is expanding the scope of the project. Ms. Payne suggested that the task force could include a research phase versus just a test criteria phase.

Mr. Dacey explained there are criteria in the auditing standards that address related party disclosures. He stated this is a challenge because it is not in the accounting standards.

Mr. Steinberg explained that he could see this as two projects with one to address the federal entity and another to address the other things out there.

Mr. Shumacher asked if the task force would be assessing the indicators and criteria for control to determine if one by itself could be sufficient to constitute control. Mr. Farrell suggested that would be part of the task force objectives.

Mr. Farrell explained the Board's input would be beneficial as staff moves forward with the task force.

CONCLUSION: Staff will move forward with forming a federal entity task force. The task force will assist in developing the proposed standard on the boundaries of the reporting entity and consolidation as well as case studies testing the proposed criteria. Staff (and the task force) will concentrate on the areas identified by Board members for consideration. Staff will report back to the Board after meeting with the task force.

- **Measurement Attributes**

The Board met for the first time on a new conceptual framework project, which will address the definition of measurement attributes and their features. The project will develop concepts but will not set measurement standards for financial reporting. The objective of the meeting was to decide on the scope of the project. Staff had provided the Board with written information about the discussion of measurement attributes in the accounting literature, as well as an update on other standard setters' projects on the topic, especially the current joint project of the IASB and the FASB.

Staff presented two pairs of alternatives for the scope of the project. First: Should the scope (1) be restricted to possible measurement attributes for items reported in financial statements (including notes) or (2) also include possible measurement attributes for supplementary information? The second alternative could be broader because the scope could include nonfinancial attributes, such as physical condition; volume; area; quantity, quality, and outcomes of services provided, etc., as well as financial attributes.

The second pair of alternatives was: Should the project (3) address only the definition and discussion of different measurement attributes (such as historical cost, replacement cost, etc.) for initial recognition or (4) also define and discuss different measurement methods? Alternative 4 could include measurement methods and re-measurement issues as well as measurement for initial reporting—for example, measurement in nominal dollars vs. dollars of constant purchasing power. The staff's recommendation was to focus on Alternatives 1 and 3 and defer Alternative 4 to a future project.

After discussion of various possibilities, the nine members present selected Alternatives 1 and 3 for the initial scope of the project. Initiating the discussion, Mr. Jackson asked whether it was possible to address Alternative 3 without also addressing Alternative 4. Staff indicated a concern that the resulting project might be too broad initially and suggested that Alternative 4 could be introduced

later in the project, if necessary, or deferred to a future project. Mr. Patton said Alternatives 3 and 4 should be addressed together. He also wondered whether there were aspects of Alternative 2 that might need to be considered in relation to the Board's Entity project, but other members and staff did not share that concern. Mr. Dacey advocated limiting the scope of the project, at least initially, because if the project was too broad at the start, it could quickly become unmanageable. Mr. Schumacher said he agreed with selecting Alternatives 1 and 3 for the initial scope, but the Board should allow for the later addition of issues from Alternatives 2 and 4 as needed.

Mr. Farrell said, given that other standard setters are addressing issues that fall within Alternatives 1 and 3, he wondered whether the FASAB should wait for their conclusions and in the meantime deliberate nonfinancial measurement attributes, such as quality, outcomes, etc. (Alternative 2) Mr. Jackson, Mr. Steinberg, and Ms. Hug (for Mr. Werfel) were interested in the measurement of the physical condition of assets, although they did not advocate including Alternative 2 in the initial scope of the project. Mr. Murphy said he was unsure how the measurement of condition would fit into the project. He was more interested in bringing into the project some aspects of Alternative 4. He would start with Alternatives 1 and 3 but keep Alternative 4 in mind. Ms. Payne said that the FASAB already has on its agenda a future project on some aspects of condition, such as asset impairment and deferred maintenance. With regard to condition, she was concerned about the breadth of measurement attribute possibilities when considering the condition of a museum artifact, vs. a weapons system, vs. a road. Mr. Farrell also was unsure that the measurement of condition would fit into the measurement attributes project.

Mr. Farrell summarized for the Board and staff that the consensus was that Alternatives 1 and 3 were the preferred starting points. There also was interest among the members in condition reporting, which staff should be aware of when working on Alternatives 1 and 3, because it might logically fit somewhere. Also, condition reporting should be on the Board's list of potential agenda items to consider at the February 2008 meeting. Notice also should be taken of the point made by some members that Alternative 4 is not or may not be separable from Alternative 3.

CONCLUSIONS: The Board decided that the project should focus, at least initially, on defining measurement attributes and their features of items that are candidates for recognition in the financial statements or disclosure in the notes (i.e., Alternatives 1 and 3). This decision does not preclude consideration of measurement attributes for required or other supplementary information (Alternative 2) as well as consideration of inflation-adjusted vs. nominal-dollar measurement methods (Alternative 4) later in the project, if these additions became advisable. It was agreed that staff would present a project plan to the Board at the February 2008 meeting.

- **Appropriate Source of GAAP**

Ms. Ranagan, Assistant Director, opened the session by summarizing the outcome of the September meeting and explaining that this session was primarily intended to be an educational session to provide the Board members with a better idea of the extent of federal financial reporting using a primary source of generally accepted accounting principles (GAAP) other than that developed by FASAB (e.g., the Financial Accounting Standards Board (FASB)).

Ms. Ranagan then presented her informational paper to the Board members. Her paper contained a listing of all of the entities required to prepare financial statements under the *Chief Financial Officers Act of 1990 as expanded by the Government Management and Reform Act of 1994 (CFO/GMRA)*, the *Accountability of Tax Dollars Act (ATDA)*, and the *Government Corporation Control Act (GCCA)* with a link to each entity's 2006 financial statements, if available, as well as the source of GAAP used to prepare the financial statements (FASAB vs. FASB GAAP) and the audit opinion received thereon. Information was also provided for some of the legislative branch entities as well. Staff is not aware of any judicial branch entities that have begun preparing financial statements.

Ms. Ranagan noted that Mr. Jacobson had pointed out to her that the Legal Services Corporation (LSC) should not be included as an Executive Branch entity. Although LSC meets the conclusive and indicative criteria from Statement of Federal Financial Accounting Concepts (SFFAC) 2, its legislation states that it is a nonprofit corporation in the District of Columbia and not a federal entity. Ms. Ranagan noted that she would defer discussion of this issue to the Federal Entity project currently underway.

Ms. Ranagan stated that an updated project schedule was included at the back of Appendix 1 and asked the members if they had any questions or concerns about the project proceeding as outlined at the September meeting.

Mr. Murphy asked why the Federal Home Loan Banks, which constitute a material government sponsored enterprise (GSE), were included on the listing of entities required to prepare financial statements under the GCCA. He inquired if they would be included in the consolidated financial report of the U.S. Government (CFR). Ms. Ranagan responded that she did not know about the status of the Federal Home Loan Banks but if they are a GSE they would not be included in the CFR unless the Federal Entity project results in different requirements than what is currently in SFFAC 2.

[STAFF NOTE: Ms. Ranagan later inquired of Mr. Jacobson the unique status of Federal Home Loan Banks, the Financing Corporation, and the Resolution Funding Corporation, all three of which are listed as government corporations in the GCCA but appear as a GSE in the federal budget and are excluded from the

CFR. He responded that Congress created the entities to help further a policy objective (facilitate lending, resolve S&L failures, etc). Congress made the entities subject to certain federal regulation and oversight and, in part, used the GCCA and the government corporation structure as the vehicle to achieve the objective. But Congress also insulated some of the financial aspects of the corporations from the U.S. Government by providing that the corporation liabilities are not liabilities of the U.S. Government and by having private commercial entities capitalize the corporate assets and fund its ongoing operations. Mr. Jacobson noted that this is truly a hybrid entity. Ms. Ranagan asked "So these are government corporations but they are not federal entities and thus are supposed to be excluded from the consolidated financial report of the U.S. Government?" Mr. Jacobson responded that is an accounting policy judgment. It is just important that you keep in mind that the government does not own or control (other than in a regulatory sense), the assets or liabilities.]

Mr. Farrell asked what Ms. Ranagan anticipated doing next and what the Board members would be presented with at the February meeting. Ms. Ranagan responded that her first step, based on the results of the last meeting, would be to determine the user needs of the entities currently reporting under FASB, develop proposed reporting requirements that would incorporate those user needs with the needs of Treasury in compiling the CFR (e.g., footnote reconciliation, Statement of Budgetary Resources, etc), and then prepare a draft survey to get feedback on the potential costs, burdens, and hurdles to providing the information necessary to satisfy the proposed reporting requirements.

Mr. Farrell asked if staff was requesting the Board members to approve a draft of the survey document before it is sent out. Ms. Ranagan responded that she had been requested by one of the Board members to let the Board review a draft.

Mr. Werfel said he thinks that is the right approach for the Board to make an informed decision, but he thinks there is one missing piece. In addition to receiving feedback on the differing levels of burden (e.g., status quo, footnote reconciliation, full conversion to FASAB), he would like to see a staff position paper that compares the pros and cons or strengths and weaknesses of the CFR in its current format to one that requires more consistency or homogeneity. He sees that as a useful part of the equation to get FASAB staff's impressions in addition to the views that Treasury has expressed. He would like to be able to look at the balance of governmentwide costs vs. benefits (e.g., additional person hours required at the agency level to meet new reporting requirements versus the person hours saved at Treasury in compiling the CFR). He would also like to be able to get a sense of what is compromised by allowing the current status quo to continue when there are a number of federal entities reporting under a different source of GAAP.

Mr. Jackson reiterated his point from a prior meeting that the needs of the users of the financial statements should be given primacy and the consolidation should

be given secondary consideration. He said we should be concerned about consolidation but figure out how to achieve it in the least burdensome way.

Mr. Reid said he would argue that the consolidation is one of the primary uses of these financial statements, maybe the only one.

Ms. Payne reminded the Board that the reason the project was initiated was because the AICPA expressed concern to us that we have a domain as a GAAP standards-setting body and, because of circumstances, we made a decision in early 2000 to grandfather and permit FASB for certain entities. Everyone is aware that it was an ad hoc decision; there was no sorting of groups by user needs. While it is permissible to determine that different groups of entities may appropriately follow GAAP for different domains, FASAB has not done that analysis.

Mr. Farrell said the answer ultimately out of this might not be forcing entities to switch to FASAB but adopting as part of our standards the acceptability of certain entities to follow standards of a different domain.

Mr. Dacey said that he had suggested at the last meeting that there be two acceptable reporting methods and entities be allowed to switch one way (i.e., prepare either FASB or FASAB and be permitted to switch from FASB to FASAB but not be allowed to switch from FASAB to FASB).

Ms. Payne reminded the members that one of the considerations that was raised in the very first staff paper on this project was that the group of FASB reporting entities is not homogeneous; there are a number of users that are used to seeing FASB information (e.g., SEC filers, bondholders, rate-setters, etc.). There are conceptual-based arguments for maintaining FASB statements in some cases as well as cost/benefit arguments that could be made in some cases. Because of the desire to avoid turning this into a full-blown project, we went down the avenue of trying to support the consolidation.

Ms. Payne said that Mr. Werfel had requested information on the cost of preparing the CFR from multiple sources of GAAP. She noted that staff would need to survey Treasury and GAO staff to obtain cost information on preparing and auditing the CFR. She asked Mr. Werfel if he was comfortable with that. Mr. Werfel said he does not know how the Board can move forward without knowing what is being spent. Mr. Reid said he would imagine that it would be more significant on those that would actually have to convert.

Mr. Reid said it would help if they could get positive assurance in the audited financial statements that there are no material differences between FASAB and FASB presentations.

Mr. Jackson asked where the significant differences are other than the valuation of investments that was mentioned earlier. Ms. Payne said that information was provided in an earlier staff paper. Mr. Reid said utility accounting at the

Tennessee Valley Authority (TVA) is the one that sticks in his mind. Ms. Payne said she differs on that because she believes regulatory assets are not property, plant and equipment (PPE) but rather are different assets and they can get to utility accounting through following the FASAB hierarchy. Mr. Reid responded that he and Ms. Payne differ from TVA's thinking on that point. Mr. Reid said that the difference between what TVA would capitalize and what FASAB would capitalize is about \$10 billion.

There were no further comments.

CONCLUSION / NEXT STEPS:

At the September meeting, the majority of the Board requested that staff further develop Option B (implement workgroup recommendation) but include additional information about financial statement user requirements for entities that are preparing FASB-based statements. Some members also requested to see a draft survey requesting cost information about the proposed changes to component level reporting. At the October meeting, staff was also asked to prepare a position paper that compares the pros and cons or strengths and weaknesses of the CFR in its current format to one that requires more consistency or homogeneity, including an analysis of the balance of governmentwide costs vs. benefits of changes as well as status quo.

Staff plans to complete the following:

- Determine the needs of the principal users of federal financial statements currently being prepared in accordance with FASB standards and whether they justify different reporting outputs from the principal users of federal financial statements prepared in accordance with FASAB standards;
- Describe the impact on the CFR of status quo versus requiring more consistent and homogeneous reporting;
- Present more information on whether the FASB permission and reconciliation requirement would apply to only those currently preparing federal financial statements or if that option would be extended to new entrants; and,
- Prepare a draft survey for the Board's review that includes options for what would be included in the audited reconciliation footnote (e.g., budgetary information vs. no budgetary information) and would be used to solicit input from the affected community on costs and burdens associated with the additional reporting requirements.

- **Initial Capitalization of PP&E under SFFAS 6 as amended by SFFAS 23**

Ms. Payne introduced the project, Initial Capitalization of General PP&E, which began as a discussion at the September 2007 meeting with the technical agenda options discussion. She reminded the Board that during that discussion the members expressed some support for an effort to reduce the cost expected to be incurred at the Department of Defense (DoD) as they establish values for general PP&E during the coming years. Ms. Payne noted to the Board that FASAB staff member Monica Valentine would be leading the project from this point on, as well as leading the AAPC phase of the project. She also mentioned to the Board that the AAPC had just voted out two technical releases (TR) that would be forwarded to the Board very soon to begin its 45-day review of the TRs.

Ms. Payne presented to the Board a draft exposure draft (ED) showing guidance that could be developed to address the issue of initial capitalization of general PP&E. She stated that there is a perception that after the implementation of SFFAS 23 in FY 2003 the “bar” had been raised as far as the estimating of general PP&E. So in order to reduce the cost of estimating the initial capitalization of general PP&E new guidance is being proposed. The draft guidance would provide relief to agencies who are not yet required to report PP&E and those who still need to develop their systems to accomplish the requirements of SFFAS 6 & 23. The proposal would give new implementers of the standards 5 years from the date an entity begins to report PP&E. The entities would be allowed to estimate PP&E under the guidelines of this standard for the 5 years while putting their systems in place to eventually report PP&E in accordance with SFFAS 6 & 23. In the absence of viable systems in place, estimating PP&E values is the only option to reporting a value for PP&E. This proposal would amend the current standards to make it clear that estimating of PP&E values in accordance with SFFAS 6 & 23 is permissible. Ms. Payne asked the Board if they wanted to staff the project to develop a standard and what areas of the project should be passed onto the AAPC.

Mr. Werfel reiterated what he envisioned as the three broad objectives for this project:

- the five-year rolling implementation period,
- the work of the AAPC, and
- a discussion for the agenda-setting session to address the larger fundamental issues of valuing general PP&E.

Mr. Patton asked what incentives do the agencies have to put the needed systems in place to track PP&E. Ms. Payne replied that her belief was that having an unqualified opinion by virtue of accurately reporting PP&E, which ultimately affects the Statement of Net Costs would serve as a motivator. Mr. Jackson noted that since the effective date of SFFAS 23 in FY 2003 through the proposed date of 2012 several billion dollars worth of military equipment would

have been acquired by DoD through its many acquisition programs. In order to meet the requirements of SFFAS 6 & 23 DoD would need to change its contractor acquisition processes, business processes, as well as its systems to meet these requirements. He reminded the Board that when DoD spoke to the Board in 2000 about the implementation of SFFAS 23 in FY 2003 they did not take due consideration of the major implications involved in such an undertaking. He also noted that DoD will need a systematic method/process to capturing their assets and that it will take several years to put in place. However, they are moving towards improving their precision in valuing military equipment.

Mr. Werfel expressed his interest in the Board also discussing the possibility of valuing PP&E at replacement cost or fair value, especially with the FASB's interest in fair value accounting. Mr. Patton asked if the proposal was essentially amending a standard even before it gets implemented. Ms. Payne addressed the commonalities between replacement cost vs. historical cost. She noted that both historical and replacement costs require acquisition costs to be captured, cost allocations, and periodic adjustments in reported values. Mr. Werfel acknowledged that whether DoD were required to report costs at historical or replacement value, the systems cost would still be great. However, he did note that the return on investment when using replacement cost is greater because it produces better valuations, more useful for decision-making, and would lead to better integration between the users of the information.

Mr. Patton cautioned the Board as it considered changing its foundational principles because a few entities find them objectionable; it could jeopardize the Board's stability and status. Mr. Werfel reminded the Board that there have been no major changes in PP&E valuation since its adoption over ten years ago. Mr. Steinberg also reminded the Board that the Board's original philosophy on DoD PP&E was to view their military assets differently than general PP&E, but DoD later asked to have their asset treated the same as other general PP&E. He also expressed a concern that the eventual guidance of the AAPC may still not produce decision useful information. Ms. Payne reiterated that the purpose of the proposed guidance in the exposure draft is not to revisit the principles of SFFAS 6, but to provide a more cost effective vehicle for the implementation of the PP&E standards.

Mr. Jackson stated that DoD is not looking to avoid the implementation of SFFAS 6 & 23, but simply needs a mechanism for orderly transition while recognizing the complexity of the implementation issues. Secondly, the Board should consider the enormous cost involved to achieve a level of precision that we are not certain was ever intended.

Mr. Werfel suggested that the Board consider a public hearing on the valuing of PP&E that would be similar to the public hearing on social insurance. Mr. Reid suggested also conducting a survey to determine what other countries use to value various types of assets.

Mr. Farrell made the point that there should not be as much emphasis placed on the level of precision on the PP&E value but look to providing a meaningful and cost-beneficial depreciation calculation. He went on to say that the Board should really take a look at ways to reduce the cost of accounting for PP&E throughout the government.

Ms. Payne noted that there appeared to be support from the Board on asking the AAPC to develop implementation guidance for PP&E. She informed the Board that staff would develop a project plan for the AAPC's work and that the Board would have an opportunity to review it. She then polled the Board on their support for the proposed exposure draft that would amend SFFAS 6 and provide guidance on how to estimate PP&E. Mr. Patton questioned the use of the 2012 date-certain as an effective date for the amendment. The Board agreed to use some other type of mechanism to trigger the full implementation of SFFAS 6 that would coincide with having systems capable of accurately tracking PP&E. Mr. Jackson suggested using the FFMI system certification as a possible benchmark. Ms. Payne also suggested using the reporting of material weakness as a benchmark.

CONCLUSIONS: Staff will develop the exposure draft further and request that the AAPC consider implementation guidance related to the issues outlined in the staff memo. In addition, the Board will consider further evaluation of the existing standards as a potential project when it considers the technical agenda at the February meeting.

Adjournment

The meeting adjourned at 4:00 PM.

Wednesday, December 5, 2007

Agenda Topics

- **Administrative Matters**

Mr. Werfel introduced a new OMB staff member, Regina Kearney.

Mr. Reid provided an update on the two Social Security issues papers provided to members. He noted that the Treasury Secretary has made it a top priority to reform Social Security and is working to build momentum for reforms that would preserve the program. A series of white papers is being developed. The first two papers were included in the briefing materials. The first paper dealt with "what could be done" and concluded that either benefits needed to be cut or taxes should be raised. The paper makes no recommendations; it simply identifies issues and options.

The second paper deals with pre-funding and Mr. Reid believes it is more challenging to understand. The conclusion is that pre-funding does not change the fundamental outcome. He noted that the magnitude of the pre-funding needed would be so large as to be unreasonable and possibly impossible. The paper addresses intergenerational transfers.

Mr. Murphy briefed the Board on CBO's recent report on health care costs. He noted that there are ideas for reforming Social Security that might be viewed as relatively painless in comparison to issues related to health care where there is an absence of such options for reform. CBO's report highlights that the health care cost issue is not driven largely by the aging population (which is approximately 10% of the increase over time). Two other factors – that we now pay a great deal less out of pocket for care than we did years ago due to health insurance and that income has increased and, therefore, we can spend more on health care – are also minor contributors to the overall problem. The main driver is the excess increase in health care costs over general costs. The CBO Director is concerned and has assigned 25% of the CBO staff to analysis of these issues. That allocation may increase to 30% next year.

Mr. Allen updated the Board regarding the IFAC World Forum held the previous day. He noted that the audience included many economists and lawyers as well as accountants. One key point was that absent convergence in the regulatory environment one would not gain much through convergence in standard setting. He found this relevant in light of the Board's discussion of convergence. One question for the panel that he participated on was whether we are capturing the economic substance of the change – the budget deficit and the accrual deficit are each missing some aspects of economic change. Mr. Allen noted that this reinforced the need for a balance sheet so that you could measure the change from year to year. Mr. Allen perceives the next two projects – Social Insurance and Fiscal Sustainability - as dealing with a great deal of what the speakers found lacking in the reporting model. He believes these projects should move as quickly as possible but not spend a great deal of time on specifics. The focus should be on objectives and a couple of options could be included in an ED. He believes that would be more productive than members working toward a single perfect answer.

Mr. Allen asked if there were objections to the updated member evaluation form. Mr. Patton inquired about the process for changing the Statement of Members Responsibilities and the additional text proposed. Ms. Payne explained that the statement is developed and approved by the Board.

Mr. Patton indicated that there was a voting component to the statement. He would like to address the issue of statements of views accompanying abstentions. Since the statement is open to change, he suggests clarifying the section on voting regarding this point. Mr. Allen did not view that as the primary purpose of the discussion but was interested in whether members wished to address the issue of voting. Mr. Farrell indicated that, since the document is open

to amendment, he would like to address the issue of voting. Ms. Payne suggested tabling this until February so that options could be developed. Mr. Allen indicated that – absent objection – we would approve the evaluation process now and keep the statement of responsibilities changes open until the next meeting.

- **Fiscal Sustainability**

The following members of the Fiscal Sustainability Task Force participated in the meeting:

Robert Anderson, Senior Economist, Office of Management and Budget (OMB)

Benjamin R. Page, Principal Analyst, Macroeconomic Analysis Division, Congressional Budget Office (CBO)

James Duggan, Senior Economic Advisor for Social Security, Office of Economic Policy, U.S. Department of the Treasury (“Treasury”)

Thomas McCool, Director of the Center for Economics in Applied Research and Methods, Government Accountability Office (GAO)

FASAB Assistant Director Eileen W. Parlow opened the discussion.

Ms. Parlow distributed copies of a letter from Rep. K. Michael Conaway (R-TX) dated November 28, 2007. Rep. Conaway, who is a member of the Fiscal Sustainability Task Force, recommended Summary Display Option C, noting that it would assist users by presenting important information in a simple and direct manner.

Ms. Parlow said that the briefing materials included a preliminary draft exposure draft (ED) with draft displays for the Board’s discussion, as well as sections on objectives and assumptions that were revised based upon Board decisions at the September 2007 Board meeting.

Objectives (including discussion of planned Treasury project)

At the September Board meeting, the Board indicated general approval for the draft objectives, with several editorial revisions that were incorporated into the draft ED. Staff asked if any members had comments on the objectives section. Mr. Allen mentioned that the task force members were invited to comment as well.

Mr. Duggan said that he was very pleased to be a part of the Task Force’s effort. He said that Treasury is currently considering a formal analysis of U.S. fiscal policy that would be comparable to studies published by New Zealand and Australia. He said that displays could be introduced into the Management’s Discussion and Analysis section of the consolidated Financial Report of the U.S. Government (CFR) at an earlier date than would be possible by the issuance of

an accounting standard by the Board, due to the necessary length of the approval process for accounting standards.

Mr. Duggan said that this effort is currently underway, and suggested that Treasury, in coordination with OMB, would generate a formal fiscal sustainability analysis that would contribute to the efforts of the Board. He mentioned that Mr. Patton had asked about the conceptual basis for this project, and said that in recent years, other countries have done extensive formal analyses of their fiscal policies. He said that the CFR is not the place for the full framework and report—that it doesn't have the room or the readership-- but that the CFR could draw from such a report. He said that the CFR normally draws from other publications and reports, and that having such a report available would assist the Board in drafting accounting standards. However, he said that he was not suggesting that the Board stop work on the project, but he suggested that the best time for the Board to draft accounting standards would be after the pilot project is completed.

Mr. Allen said that he believes that the Board should address the issue as quickly as possible, and although he would be willing to consider Treasury's pilot project as a part of due process, he believes that the Board should not delay its work on this issue, while still taking advantage of Treasury's expertise.

Mr. Reid said that the FY 2007 CFR (due to be released on December 17, 2007) will include a much more robust presentation of sustainability issues relative to the Statement of Social Insurance, and additional information in the MD&A. He said that most of the Board's objectives are either met or can easily be included. He said that Treasury does not need an accounting standard in order to include this information in the CFR. He said that a standard would be needed to flesh out issues that Mr. Duggan was describing. He said that a draft prototype report, due for release in January 2008, would be important in determining objectives and the reporting to support the objectives.

Mr. Allen agreed that Treasury has discretion in adding material to the MD&A, but that there is a possibility that the requirement would be for a principal financial statement, not necessarily limited to the MD&A. He said that he still believes that the Board should continue its work.

Mr. Werfel said that he believes there is value to having a principal financial statement, in order to strengthen the reporting. He believes that a pilot would be valuable research, but that a principal financial statement in addition to coverage in the MD&A would be extremely important. He said that such a financial statement might be the most important financial statement in the CFR.

Mr. Reid said that it might be easier to address questions, such as the content of the information and its placement within the CFR, when the report becomes available. Another item would be if a "bottoms up" analysis, based upon information from agencies, would be helpful.

Mr. Jackson said that he likes the notion of a prototype. For example, one of the Options in the draft ED- would be helpful to the Board in determining the relevance of the information. He said that although he is enamored of the idea of a principal financial statement, there would be enormous implications for auditing the information. For example, one implication would be testing the reasonableness of assumptions.

Mr. Dacey said that it sounds like there will be a concurrent process, and said that the information flow will help both projects. He said that it will be helpful to have a report similar to the Trustees Report but with broader scope. He said that he is confident that GAO will be able to issue an opinion on the SOSI. He said that in terms of auditing the reasonableness of assumptions, he supports the idea of a primary display with alternate scenarios to explain the range of outcomes, which would make it easier from the audit standpoint.

Mr. Allen said that it is important not to imply more precision than is possible in the report.

Mr. Farrell said that although it is important for the U.S. to have a full report similar to that of other countries, but said that he believes that there should be something in the CFR as quickly as we can get it there, and that he is concerned that if the Board does not move concurrently, valuable time could be lost if, for example, the management view at Treasury changes and the Treasury “prototype” effort altered or stopped.

Mr. Werfel agreed, and said that an accounting standard could assure consistency in the reporting.

Mr. Farrell asked Mr. Duggan about the planned timeframe for the report.

Mr. Duggan said that he would have to work it out with Mr. Reid, but that the summer of 2008 was a possibility for a draft report.

Mr. Schumacher asked if Mr. Werfel believes that the Board should continue its work while the Treasury pilot report is developed.

Mr. Werfel said that he believes that the Board should continue its work, and that the Task Force should move forward. He said that he does not wish to constrain the work of the Task Force, and said that the Board should ask the Task Force what is needed from the Board in order to support the work of the Task Force.

Mr. Duggan said that Treasury intends to communicate regularly with the Board, but that he believes that the Board should not place constraints upon Treasury in its work on the pilot project.

Ms. Parlow said that the Task Force is quite a large group, and that the initial request when recruiting Task Force members was to get expert comments from the Task Force on specific issues, such as assumptions and displays, and subsequently to review materials drafted by FASAB staff. The Task Force was not tasked with reaching a consensus on all issues discussed, but rather to explain the pros and cons of specific issues so that the Board could consider those pros and cons in its deliberations. Ms. Parlow said that the Task Force is not a standing body of compensated individuals—they are primarily volunteers.

Mr. Allen asked if Mr. Duggan's concern was that the Board might constrain Treasury in its work on the pilot, or whether Treasury believes that the Board's objectives are improper.

Mr. Duggan said that he believes that the Board is going in the right direction.

Mr. Page asked Mr. Duggan what new information would be provided by Treasury's project.

Mr. Duggan said that Treasury wants to produce a developed conceptual framework that would be based upon the intertemporal budget constraint that translates into a present value borrowing constraint, which allows discussions of fiscal sustainability to have meaning. He said that the goal is to provide indicators that are easily explained and useful for policymakers. He said that the idea is not so much new data, although there would be some new projections for Medicaid and the rest of government, but that the focus would be on the major social insurance programs, at least at the start. For example, you know that increasing debt in proportion to GDP is not sustainable, but what is the point at which it becomes a problem? And what needs to be done in order to satisfy the objective, to satisfy the intertemporal budget constraint? He said that the development of such a framework would not belong in the CFR, but would be useful to policymakers.

Mr. Allen suggested that the Board proceed to staff's questions regarding the draft ED, keeping in mind Treasury's concerns.

Mr. Allen asked if there were any problems with the objectives.

Mr. Patton said that he was concerned about a definition for fiscal sustainability, and said that he believes that the Board does not have a firm or clear understanding or definition of the term "fiscal sustainability." He said that if the Board does have a firm definition, that it should be provided to the Task Force members for their use in the project.

Ms. Parlow said that the term "fiscal sustainability" was first introduced to the Board as the title of a pro forma financial statement in the Alternative View of

Preliminary Views, Accounting for Social Security, Revised.² She said that there is no internationally agreed-upon definition of fiscal sustainability.

Ms. Payne said that there are no internationally-accepted set criteria, such as a percentage of debt-to-Gross Domestic Product (GDP), for “fiscal sustainability.”

Mr. Dacey said that there is a distinction between “fiscal sustainability reporting” which helps the readers assess, in their own minds, fiscal sustainability, but that defining what is fiscally sustainable is something that the Board really can’t do, unless the Executive Branch puts out a policy directive.

Mr. Anderson agreed that there is no particular level of debt-to-GDP that could be defined as fiscally sustainable or not (except for very extreme cases). He said that he wanted to get back to Mr. Duggan’s point about the economic concept of the “intertemporal budget constraint.” He said that using projections, you can say that the intertemporal budget constraint is satisfied or not, so in that sense you can define fiscal sustainability. But there might be quite a wide range of debt-to-GDP ratios that could satisfy that constraint, so you can’t come up with a particular number. He said that this might be what Mr. Duggan described as a conceptual framework.

Mr. Patton said that he wanted to know if it’s universally true that situations such as permanent deficits and rising debt-to-GDP are generally accepted parameters for fiscal sustainability. He asked if Australia’s definition might be an alternative or another dimension and why it did not appear in the Objectives section.

Ms. Payne quoted Australia’s definition:

Fiscal sustainability is the government’s ability to manage its finances so it can meet its spending commitments, both now and in the future. It ensures future generations of taxpayers do not face an unmanageable bill for government services provided to the current generation.

Ms. Parlow said that at the September meeting, a member asked to have Australia’s definition moved to the Basis for Conclusions because it was Australia’s definition and is presented as background information rather than a definition that the Board adopted as its own definition.

Mr. Patton asked if the Board agreed that the point of the reporting was to provide information that would allow the reader to assess whether there are likely to be permanent deficits and/or rising debt-to-GDP levels. He asked if that wording (in paragraph 8 of the draft ED) was the Board’s operational definition.

² Available at www.fasab.gov

Ms. Parlow said that another way of saying that is [FASAB's] sub-objective 3B in SFFAC 1:

Federal financial reporting should provide information that helps the reader to determine whether future budgetary resources will likely be sufficient to sustain public services and to meet obligations as they come due.³

Mr. Patton asked if the members believe that paragraph 8 of the ED should be the Board's operational definition of fiscal sustainability.

Mr. Farrell said that paragraph 8 opens up "intergenerational accounting."

Ms. Parlow said that the Board could expand the scope of this project to include intergenerational accounting, but has not yet addressed this option.

Mr. Anderson said that there were two questions: you can say that something is sustainable, but also you might ask if it's fair, which is a lot harder.

Mr. Farrell said that every time you see a report like this, you see a disclaimer to the effect of "but this will never happen, because the government will change its policies."

Mr. Anderson said that what it means is that if the government doesn't change policies, then at some point you're not going to pay your bills, which we've never done as a government, which leads people to the conclusion that something will be done to fix it. It would be a pretty drastic thing to conclude, that you weren't going to pay your bills.

Mr. Murphy said that at some point, nobody will lend us money.

Mr. Anderson said that this has happened in other countries, but fortunately not in the United States. What happens usually is that the government starts to print a lot more money – they use their monetary powers. They're not finding willing lenders, so they just print more money and you have hyper-inflation. That's happened at different times in the 1980s in different countries, in Latin America and in Europe at different points.

Mr. McCool mentioned a recent Standard and Poor's article.

Mr. Anderson said that the chief economist at Standard & Poor's, David Weiss, did some long-run budget projections like OMB and CBO have done, and he concluded the same basic point that we all come to, although he was a little more aggressive in his timing, that if you don't change policies you're not going to be able to pay your bills. But if you talk to the people at Standard & Poor's who do

³ SFFAC 1, paragraph 139.

the credit rating, that is not David's job, and they still rate U.S. debt as triple-A, and it's as good as any debt in the world, so it's very misleading to go out there and say that "Standard and Poor's" in some sense is down-grading U.S. debt, because that's not true.

Mr. Patton said that if "sustainability can be assumed if current policies are unlikely to lead to permanent deficits and rising public debt as a share of GDP," so is that the operational definition of sustainability that the Board wants to work with.

Ms. Payne said that there is an important footnote, that determining precisely how much a government can depart – in magnitude or duration- from this general notion of fiscal sustainability is beyond the scope of the Board's efforts.⁴ There is another important footnote that notes that fiscal sustainability reporting does not extend to supporting a detailed assessment of whether current policies are optimal; rather, it addresses the fiscal outlook if current policies are continued.⁵

Mr. Anderson said that he would re-word the paragraph 8 to describe fiscal unsustainability as being assumed if current policies are likely to result in permanent deficits rising public debt as a share of GDP, because some people might want to bring into the notion of "sustainability" other elements such as fairness, or optimality that we were talking about earlier, so that finding a situation that can be described as "sustainable" might be more difficult.

Mr. Allen said that paragraph 8 seems to be as close as we can get to an operational implementation of a definition without actually being a formal definition. Maybe that's all we can do. He said that he is not concerned about the fact that, like Australia, we are dealing with a notion- we're not dealing with something that can be neatly bound up as a definition in a couple of sentences.

Mr. Patton said that it's not a good idea to start a key element, such as sustainability, with an explanation that starts with the word "generally." He said that this is too ambiguous for a standard-setter to do.

Mr. Dacey said that he is concerned with paragraph 8 and does not think that it should be part of the Objectives. He does not think that paragraph 8 adds a whole lot of value to what has already been said in paragraph 7. He asked if paragraph 8 should be moved out of the Objectives section, perhaps to somewhere else in the document.

Ms. Parlow said that she is concerned that previous Board discussions have concluded that the concept of fiscal sustainability cannot be defined in a precise way—that doing so would be extraordinarily difficult and would likely imply setting

⁴ Footnote 14, page 10 of the draft ED (Attachment 1 of the December 2007 briefing materials).

⁵ Ibid, Footnote 12, page 10.

budget rules, which is not the Board's domain. She said that the "plain English" meaning of the term "fiscal sustainability" might make it a useful and intuitively meaningful term, but if not, the term could easily be deleted from the draft ED. Paragraph 6 of the ED suggests explaining the term "fiscal sustainability reporting" as a useful term to refer to "comprehensive long-term fiscal projections and accompanying narrative and graphics to be provided in the CFR."

Mr. Allen said that "fiscal sustainability" is a notion, and that's as far as the Board can go- you can't have a prescriptive definition.

Mr. Farrell said that you're not reporting on "fiscal sustainability" per se- you're giving indicators of fiscal health, you can provide a "statement of fiscal health" and people can draw their own conclusions.

Mr. Parlow said that this would raise a similar question of "what is fiscal health"- that we can tie ourselves in knots. She said that staff is ready- in order to move forward with this project- to simply drop the term "fiscal sustainability" from the ED, which can be easily done, if the Board so wishes. She said that the term could be revisited later, after the Board has concurred on potential summary displays, and/or the potential placement of displays. She said that the Board has indicated that it really wants to get something done on this project, and expressed concern that the Board could easily spend a year deliberating on a potential definition of "fiscal sustainability."

Mr. Patton said that "fiscal sustainability" is a central concept, and you can't ignore a central concept and build it on sand.

Mr. Reid said that the term "fiscal sustainability" has a kind of generally-accepted sort of usage, that it's being used by other countries, and that it's certainly going to be recognized. When you issue a report, those words are going to mean something to people who are likely readers.

Mr. Dacey said that he likes the term "fiscal sustainability reporting" and is fine with using the term, for the reasons that Mr. Reid expressed. He said that trying to define "fiscal sustainability" is an entirely different question. He said that the objective of the project is to provide information as discussed in paragraphs 6 and 7 of the draft ED.

Mr. Allen asked if the Board wishes to adopt Australia's definition as its own definition.

Mr. Reid said that Mr. Patton and Mr. Duggan were both suggesting that we need some fairly concrete parameters here, but we may not know the range of those parameters. In other words, we're going to start here, and say that fiscal sustainability means this, but maybe there are shades of gray here, and the shades of gray are what's likely going to be fleshed out by the report itself, and

there are things we're going to learn as a result of doing that, that may impact that definition. For example, if the shift of costs from one generation to another is one of the indicators, but it may be a situation where you haven't gotten to edge of the precipice and fallen off the edge, but you've definitely shifted costs out of generation A into generation B, or maybe from B to C and so on, you may be in a situation where you're getting darker and darker shades of gray with regard to this, even though you haven't gotten to this view that says it's fiscally unsustainable. And that's where, now, do you really have a fiscally unsustainable situation, because you're getting ever grayer with regard to future generations, are you making the quality of life there something that's radically different from what we have today. And that's why I think that maybe looking at this, is it really an on-off switch, that says that it's fiscally unsustainable or not, or are there situations where there are other conclusions that don't go all the way to "unsustainable" but clearly go to "undesirable."

Mr. Allen said that rather than spend a lot more time on this- at the last meeting, no members objected to Australia's definition-- could we say in our standard that this is the notion or concept that we're moving to, and that's as far as we need to go right now, because in our due process with an ED we'll be seeking feedback. He said that he doesn't feel that the Board needs a precise definition of "fiscal sustainability" in order to move forward. He said that Australia did a good job of capturing the notion, even though "unmanageable" was not defined, but it's a notion that people understand.

Mr. Werfel said that the term does have a plain English meaning and that people can relate to it. He said that there is a framework that you can't continually increase borrowing as a share of GDP, that there's a domino effect. He does not believe that the Board needs to define "fiscal sustainability" in order to inform the public about the implications of rising debt-to-GDP levels.

Mr. Reid agreed, and said that the objective of the reporting is to answer questions, to shed light on issues.

Mr. Dacey said the International Public Sector Accounting Standards Board, at its meeting the previous week, did not go beyond what's covered in paragraphs 6 and 7 of the ED. He said that there was some discussion at the table, similar to the discussion the Board has just had, and the decision at that meeting, which was at the "project brief" level, was not to try to define "fiscal sustainability" but rather to define the objectives of the reporting, and those objectives were targeted to the same objectives as those in paragraphs 6 and 7 of the draft ED.

Mr. Patton said that he wanted to make sure that we have agreement on the dimensions of how the extent of sustainability will be measured, and an operational definition that would include permanent deficits and rising debt-to-GDP. He asked if those things were elements that the Board wants to provide information about to help people assess sustainability.

Mr. Allen asked if there were any objections. There were none.

Ms. Parlow asked if there was a consensus on specific edits- for example, to delete the word “generally” from paragraph 8, and/or to re-word it to define “unsustainability.”

Mr. Jackson asked whether paragraph 8 is even necessary. He said that he is concerned with what fiscal sustainability reporting should measure. Mr. Steinberg and Mr. Dacey expressed concern that paragraph 8 goes beyond what is described in paragraphs 6 and 7.

Mr. Murphy said that he agrees with those members who would drop paragraph 8 altogether. He said that for one thing, the idea that permanent deficits per se indicate a lack of sustainability was open to question and recommended that the reference to permanent deficits be deleted.

Ms. Parlow said that staff would strike “permanent deficit,” asked about rising public debt as a share of GDP as an indicator, and mentioned that there appears to be a difference of opinion among the members about whether the draft ED should omit paragraph 8 or whether it should include some version of it.

Mr. Allen said that the Board seems to agree on the substantive issues, and asked that staff work with members via e-mail to finalize the wording of the objectives and reach consensus on a working definition so that the Board could proceed to other topics.

Mr. Steinberg said that most financial statements are management’s assertions, but that this reporting would include some kind of analysis as to what can be done. He said that he is wondering whether the objectives should reflect this.

Mr. Allen said that the Board could address this as it develops specific requirements. Mr. Steinberg said that this would be acceptable.

Staff agreed to work with members via e-mail to finalize the wording on objectives and to reach consensus on an operational definition of fiscal sustainability.

Assumptions

Ms. Parlow said that at the September 2007 Board meeting, the members indicated that the ED for a proposed Statement should include broad guidelines for assumptions rather than detailed rules, and that assumptions for projections should be consistent with current levels of benefits, services and taxation, and that the economic assumptions for fiscal sustainability reporting should be consistent with the economic assumptions used for Social Security and Medicare

in the preparation of the SOSI. She said that the draft ED reflects those Board decisions.

Mr. Steinberg said that someone in the government should be setting the economic assumptions for the entire federal government, and that Ms. Parlow has replied that at this time there is no single authority. Mr. Steinberg said that since Treasury would be the preparer for fiscal sustainability in the CFR, he believes that economic assumptions could be set by Treasury.

Mr. Anderson said that OMB makes economic assumptions for the whole of government, but that the horizon for those assumptions is only 10 years, and in the current administration OMB is only publishing economic assumptions for the next 5 years. He said that the Social Security actuaries make economic assumptions for the Trustees Report, and those assumptions do go out over a long period of time. So, you have two sets of assumptions. And CBO also puts out economic assumptions.

Mr. Steinberg said that since Treasury puts out projections in the front of the MD&A [of the CFR], where is it getting the assumptions?

Mr. Werfel said that Treasury is using the information from the SOSI, which is based on the assumptions that were used to generate the Trustees Report.

Mr. Steinberg said that you are then basing your assumptions on the SOSI, on the Trustees Report for the government's assumptions.

Mr. Farrell said that they are the biggest numbers, and you have one set of audited assumptions, you don't want the fiscal sustainability reporting to be based on some other set of assumptions.

Mr. Steinberg said that he was simply surprised that the federal government puts out a report that doesn't have its own assumptions, that simply accepts an agency's assumptions.

Mr. Duggan said that the assumptions are not the actuaries' assumptions, that they are the Trustees assumptions. He said that the managing trustee is the Secretary of the Treasury, so in that sense, when acting in the capacity of Trustee for the 75-year period, in that sense, they are Treasury's assumptions.

Mr. Murphy asked about the projections for Medicaid. Mr. Duggan said that there are no special rules for projecting Medicaid, as compared with any other part of the budget- that projections used rules-of-thumb, such as proportionate to GDP. Mr. Anderson agreed, and said that the Medicaid budget is projected for 10 years just like any other agency's budget, and that's based on the administration's economic assumptions. He mentioned that there has always been an inconsistency between the projections for Social Security and Medicare in the

budget versus the Trustees Report, but that this inconsistency has always been there.

Mr. Murphy asked if there are projections for 75 years. Mr. Anderson said that there are no specific projections for Medicaid beyond 10 years.

Mr. Allen asked if CBO does long-run projections for Medicaid.

Mr. Murphy replied that CBO does, but that they are not audited.

Ms. Parlow said that spending projections for Medicaid require policy assumptions. She said that based upon the Board's decision at the September 2007 Board meeting, paragraphs 26 and 27 of the ED give the preparer some discretion in selecting assumptions that would project the continuation of current levels of spending. This is the level of guidance that the Board indicated at the September meeting.

Mr. Dacey said that somewhere around paragraph 24 there should be a broad statement of the overarching principle. He said that it's not good to allow too much preparer discretion—although this has not yet been a problem with SOSI.

Mr. Reid said that there is a robust vetting process for the SOSI assumptions with regard to the Trustees, including every four years, a review by professional organizations of actuaries; they have data that goes back for generations, and all that data is available.

Mr. Dacey said that he believes that the SOSI requirements have some criteria for assumptions, and that any such language in the standard should be imported here.

Mr. Reid said that there is no need to re-invent the wheel and that he would be more inclined to say that if you have situations that vary from what is required by existing standards in terms of assumption-setting, then you need to talk about that. Otherwise, there is no need to repeat anything.

Mr. Farrell asked if 45 days is enough time to obtain all the data necessary, or whether the latest available information could be used.

Mr. Dacey said that there is an earlier valuation date for social insurance, which allows time to develop and audit the information.

Mr. Allen said that although he would like the requirements to be as prescriptive as possible, he doesn't think that the Board should spend a lot of time on the details of the assumptions requirements, because the exposure process would indicate issues of concern.

Mr. Patton asked whether Mr. Dacey's idea of multiple scenarios ought to be built in as a requirement. For example, paragraph 32 (d) mentions "alternative scenarios where appropriate," which could be made more specific.

Ms. Parlow said that she will be able to do so when the Board approves specific items to be included in the proposed reporting. She said that specific requirements for alternative scenarios are already embedded in many of the items in the draft ED, but that it would be difficult to come up with a blanket rule absent Board discussion of the specific content of the reporting. For example, the proposed display of health care costs requires a range rather than point estimates, so in that instance the alternative scenarios are incorporated into the primary display.

Mr. Schumacher asked about sensitivity analysis.

Mr. Dacey said that there is a distinction between alternative scenarios and sensitivity analysis and the Board needs to determine what kind of different scenarios or sensitivity analysis would be appropriate for specific displays.

Mr. Allen asked Mr. Reid if the expanded MD&A that Treasury is currently preparing includes alternative scenarios.

Mr. Reid said that the big numbers are all from the Trustees Report for social insurance.

Mr. Anderson said that there are space constraints in terms of including information in the CFR, but that Treasury's proposed separate report would be able to provide depth of coverage of alternative scenarios and sensitivity analysis.

Mr. Patton asked about staff's question on whether to mention the concept of conservatism in paragraph 28 of the draft ED. He said that there is a mixed message in paragraph 28.

Ms. Parlow agreed, and said that the private sector (as cited in the footnote to paragraph 28) has tried to balance the concept of conservatism by explaining that reporting entities should not endeavor to report the worst possible assumptions.

Mr. Patton asked if the intent was to require an unbiased estimate, and if so he would like that to be clearer.

Mr. Jacobson said that the paragraph could simply state that the objective is to provide an "unbiased" estimate.

Mr. Allen said that in accounting textbooks, the concept of conservatism is a biasing factor, so if we are saying “unbiased” we might want to remove that concept.

Ms. Parlow asked if it would be agreeable to the Board to remove mention of the concept of conservatism from paragraph 28 of the draft ED. There were no objections. Mr. Jackson noted that paragraphs 27 and 28 could be combined, with removal of some of paragraph 28.

Per Capita Measures

Mr. Allen asked the Board to address staff’s question about limited “per capita” measures. Ms. Parlow said that the pros and cons of per capita measures were presented on pages 4 and 5 of the December briefing memo.

Staff recommended that two types of per capita measures not be presented due to objections from many of the technical members of the task force:

- (a) Per capita measures that present summary information for a certain time horizon- for example, 75 years- but use the current population as the denominator, which would imply that the current population is responsible for funding shortfalls far into the future, and
- (b) Per capita measures for infinite-horizon summary amounts, due to the difficulty of determining a reasonable population denominator.

Staff recommended that Board consider the two per capita measures in Option C:

- (a) Per capita measures of historical information, using the population numbers as of the historical date. For example, the national debt could be calculated at the reporting date and prior periods using estimated population numbers for the date being reported.
- (b) Per capita measures for finite horizon periods, using the total estimated population for the entire projection period.

Mr. Allen said that he would like the ED not to preclude or omit any specific displays of measures, but rather to say that the Board has considered them and here are the pros and cons and request comments from the public. He said that he doesn’t want to preclude any thinking. He said that he believes that the national debt per capita is precise but meaningless, because most of the imbalance occurs in the future. He said that he prefers less precision but more inclusive reporting.

Mr. Murphy disagreed, and said that he thinks that per capita numbers are false numbers, and said that their only purpose would be to scare people. He asked the technical members at the meeting to comment.

Mr. Anderson said that, as staff noted in the pros and cons, there was a pretty strong division of views among the Task Force members. He said that he personally would not include per capita measures. Mr. Duggan concurred with Mr. Anderson, and said that GDP was a more meaningful measure.

Mr. Page said that when you divide by population, you're not taking into account the fact that in 75 years people are going to be a lot better off than people today. To put these numbers into today's terms, people are going to compare them with their own salaries and it's just misleading.

Mr. Allen noted that he understood the points of technical members, but said that it is likely that the average citizen may not be familiar with the concept of GDP, and asked if there might be anything else besides per capita measures that the average citizen could relate to or understand.

Mr. Murphy said that communication is very important, but that we need to listen to the technical people who say that a certain measure is not meaningful. He said that he was troubled that staff recommended any per capita measures for consideration.

Ms. Parlow explained that per capita measures were recommended by the three Board members who drafted the pro forma "Statement of Fiscal Sustainability" that appears in the Alternative View of the Preliminary Views document, *Accounting for Social Insurance, Revised*, and that accordingly, staff needed to develop the issue for consideration by the rest of the Board members. Staff said that Option C includes the two per capita measures that are the least objectionable on technical grounds. In particular, the national debt measure is non-controversial, and it does impact the forward-looking information because it provides important information about the starting point of the projection period(s).

Mr. Jackson said that the minute you put in any per capita measure, it may set the stage for rippling through the entire document for out-year measures.

Mr. Schumacher said that he is not fond of per capita measures because he is not really sure what they mean. In other words, if the fiscal imbalance is \$40,000 per capita, is that good or is that bad? He said that maybe we should show it as a change from one year to another, so whatever measures we have we need to be able to explain them. He said that he is not sure about per capita measures, and feels that the narrative is what's most important. He said that if the economists are saying that it's not a meaningful number, then we should be careful about putting it into the reporting requirements when we can't clearly explain them.

Mr. Jackson mentioned that even for the national debt figure, it's not as if the amount is going to be spread equally among every member of the population, due to differences in ability to pay.

Mr. Farrell said that he thinks that we need measures that the average citizen can understand, and he can't think of what such measures would be, but he thinks that per capita measures would only be, as Mr. Murphy said, a "scare tactic."

Mr. Werfel said that he agrees with the members who have concerns with per capita measures. He said that he isn't sure that it's the Board's role to come up with figures that the media can use, because the media will do that anyway. He said that the Board should get out the best possible analysis and do our best to help the taxpayer understand it and put context to it.

Mr. Dacey said that in drafting the Alternative View, the challenge was to come up with measures that would convey and communicate, and that the Comptroller General uses such measures frequently. He said that he is aware of some of the technical challenges raised, but that context is important. He said that he is not sure if the ED should specify exactly how context for the information should be provided. He said that if the Board decides not to include per capita measures, that the Basis for Conclusions should explain why they were not included if the Board gets to that level of detail.

Mr. Patton said that the Board's current working definition of fiscal sustainability is focused on debt-to-GDP levels, then that's what the focus should be. He said that he would only consider per capita measures if they were highly correlated with debt-to-GDP levels.

Mr. Allen said that the Comptroller General's presentations use per capita measure because they resonate with people. For example, one of the slides shows the current average household share of debt. He noted that this is "misleading" in the sense that there is not an "average household" that will align with that average. But it's a perspective, and one can look at change in that over a ten-year period of time. One can get some perspective on this projection. Although there are technical shortcomings, there is also real value in the perspective that per capita measures provide. He does not want to prohibit the use of per capita amounts.

Mr. Duggan said that there is meaningful information in the Trustees Report- for example, that the actuarial imbalance for 75 years [for Social Security] is roughly 2% of payroll. He said that perhaps the challenge is to come up with an explanation of GDP that is understandable. He said that the objective of the CFR should be to provide information, and not to provide numbers that have serious interpretational problems—for example, by using the current population for the 75-year shortfall.

Mr. Steinberg said that we want to personalize the information, but the Board should present the information in a neutral manner, and the media and others can interpret it in different ways.

Ms. Parlow said that she would look for ways to use the “percentage of payroll” option in lieu of per capita measures.

Mr. Page said that you could also measure by what percentage revenues would need to be raised, or spending decreased, in order to balance.

Ms. Parlow said that it sounds like there is a Board consensus to find alternatives to per capita measures. The members indicated agreement.

Summary Displays

Ms. Parlow asked for members’ initial impression of the three options for summary displays (pages 6-12 of the December briefing memorandum and paragraphs 35-41 and Appendix B pages 33-41 of the draft ED).

Mr. Allen said that he would like to leave as many options open for public comment as possible.

Mr. Dacey asked if there were any attributes or characteristics of any of the options that members found appealing.

Mr. Jackson said that he finds Option B appealing because you can see change over time. He said that he also finds Option C and Option A appealing in their simplicity, but they also might be “too simple” and not answer the question of “when do we have a train wreck”? He said that Option C tells him that we are going to have a train wreck, sometime between now and 100 years, but not whether it will occur during the lifetime of his generation.

Mr. Anderson said that Option B is a really complicated construct. He said that it takes the whole present value pulled up to the front and you see how that present value evolves. What Mr. Jackson wants to see is the how the flows of receipts and the deficit and the debt evolve as you go forward. He said that it would be like putting numbers in the chart in the MD&A that shows that the debt keeps rising over time. He said that we don’t actually do that in any of these options, because they are all present value.

Mr. Jackson said that he wasn’t looking at the way the numbers are calculated so much as the basic presentation. He said we could come back later to deal with present value numbers. He really likes the presentation, the way it shows change over time. He said that he finds graphs and charts difficult to interpret.

Mr. Anderson said that OMB does a chart that goes out in 20-year increments. He said that Part 1 of Option B ends in 2012.

Mr. Jackson agreed, but noted that Part 2 goes further out, and you could always make changes to get whatever projection period that you want.

Mr. Dacey said that members should keep in mind that the Board is considering a primary summary display and a lot of supporting graphics that will show when these cash flows occur. He said that Options A, B and C are all bottom-line present value numbers, but that the supporting graphics show the timing of how differences emerge and when things really get big. He said that we should look at a combination of things, the universe of presentations that we likely need to do that.

Mr. Page said that among the Task Force technical experts, an OMB table⁶ was very popular. He said that you could tell not only when things were getting bad, but which programs were increasing. He said, however, that it's a big table and so there was some concern about how meaningful it would be to financial statement users.

Mr. Jackson said that the generations need to know if and when they're affected and who's going to be there when the door slams.

Ms. Payne brought Table 13-2 up on the screen (available at <http://www.fasab.gov/conceptssustain.html>, July 2007 "Transmittal" page 7).

Ms. Parlow explained that one of the technical Task Force members said that this table has a wealth of information for all the technical experts who are sitting around this table, but we already know about this-- but this table would mean absolutely nothing to the general public. For this reason, staff included the "bottom line" of Table 13-2 as a graph (Illustration 3a, page 47) of the draft ED. She said that if members look at the table of numbers and then at the graph, the graph is more reader-friendly. Mr. Jackson agreed that this particular graph is straightforward and easy to understand. Ms. Parlow said that although the Board indicated a desire for a summary display as a potential financial statement, the supplementary information in the ED was critical and perhaps even more important than the data in the primary summary display. She said that different kinds of information may be best presented in graphics and narrative. In particular, there is a graph in page 44 (Illustration 1b) that is a new graph from the CBO⁷ that shows the projected increase in spending on health care and it shows that the ageing of the population is nowhere near as large a factor in rising costs as was originally thought. This is why staff took the graph of population demographic trends and made that number two instead of number one, since the

⁶ Budget of the U.S. Government, FY 2008, Analytical Perspectives, Chapter 13, "Stewardship," Table 13-2.

⁷ Congressional Budget Office, *The Long-Term Outlook for Health Care Spending*, November 2007, graph on cover page and on page 14.

most important and material information should come first. The projected increase in health care spending is much larger than that of Social Security, and when you look at the increase in health care costs [as a share of GDP], the effect of population ageing is nowhere near as significant a factor as was previously thought.

Mr. Werfel agreed that the health care graph (Illustration 1b on page 44) is helpful because it brings into focus that health care is “the elephant in the room.” The graph includes Medicaid, which is not as directly impacted by population ageing as Medicare because Medicaid is not a program specifically targeted to the elderly. He said that he does not think that the table of the top ten foreign investors in U.S. Government debt (Illustrations 3c2 and 3c3 on pages 50-51 of the draft ED) are necessary. He said that the concept of the “disadvantages of delaying action” is something that he would liken to per capita measures. He said that the preparer (Treasury) or the auditor (GAO) might want to talk about the disadvantages of delaying action, but he believes that it is beyond the Board’s scope to get into that type of disclosure.

Mr. Allen asked if Mr. Werfel has a preference for a primary summary display.

Mr. Werfel said that he believes that Option C is the most preferable summary display.

Mr. Dacey said that he would like to offer a variant of Option C after other members indicated their preferences.

Mr. Patton said that he believes that some variation of Option B is useful. He would like to see projections that go further out. He would like some way of indicating that projections become more uncertain the further out in time that you go.

Mr. Allen asked Mr. Patton if he was primarily focused on flows- for example, taking the graph on page 48 of the draft ED and providing amounts, such as percentage of GDP or present value dollars. Mr. Allen said that he likes the graph very much. He said that he believes that showing the change over a longer period of time almost outweighs the value of comparing where you are this year as opposed to last year. Mr. Allen said that he would like that element incorporated into the primary summary display.

Ms. Payne addressed Mr. Patton’s comment and said that there are options for addressing uncertainty to be discussed at future meetings.

Ms. Parlow mentioned that for the February 2008 Board meeting, FASAB staff hopes to provide numbers rather than XXX for any of the Options in which the Board expresses interest. This would be helpful to the Board in evaluating the options, but would entail a lot of work.

Ms. Payne noted that there was some difficulty in obtaining information for comparable time periods- for example, some of the graphics use different sources and time periods than others. She said that CBO might be able to provide the projected amounts for the display options based on their upcoming long-term projections. She said that staff will explore the options with CBO.

Mr. Allen said he likes Treasury's Issue Briefs 1 and 2 on Social Security reform, that show how you do depending upon when you entered the system, that this inter-generational information is very helpful for getting people's attention, for example in 30-year generational segments. He said that he thinks that people can relate to that more than just a line that swings up at the end.

Mr. Farrell said that he wanted to address Mr. Werfel's comments about the disadvantages of delaying action—that the impact of changes becomes more severe if action is delayed. He asked if Mr. Werfel does not want the reporting to address that.

Mr. Werfel said that this should be left to the discretion of the preparer, who might wish to include an analysis in the MD&A, but that the Board should not require it. He said that this struck him as a "red flag" that the Board would be going outside of its scope.

Mr. Farrell asked Mr. Werfel about Mr. Page's suggestion, to report things as a percentage of payroll or GDP. He said that the Comptroller General often speaks about the cost of delay, the increased severity of the changes that would be needed. He said that this appears to be an important issue. He said that otherwise, the reader might get the impression that no action need be taken until far into the future.

Mr. Werfel agreed, and said that it is a fine line. He said that a table or graph showing things worsening over time, he'd be open to that.

Mr. Patton said that he doesn't have a good handle on the relative size of the "rest of federal government" compared with, for example, social insurance.

Mr. Reid said that most projection assume "rest of government" to maintain a constant relative share of GDP. He said that this may or may not be a good assumption.

Ms. Parlow said that projecting "rest of government" is not a simple task, and that the narrative is needed to explain the assumptions and how options for addressing the issue may become more limited in the future. For example, if "all other" is being held to a constant share of GDP as interest rises, everything else would need to shrink.

Mr. Reid said that one of your assumptions is that management can hold those numbers to that value.

Mr. Murphy said that people expect a certain level of government services, such as roads, you can show that if the government grew at a certain rate, then all of a sudden there wouldn't be any money left for any of those other services.

Mr. Anderson said that in the area of delaying action, there's a subtlety to those numbers. He said that the problem is out there. It doesn't get any bigger, but we're one year closer, and because of discounting, the number gets bigger so the readers may get a different impression, so you have to be careful in how you describe this.

Mr. Duggan said that the real cost of delay is that the longer you delay, the more cohorts are being excused from sharing the problem.

Mr. Steinberg asked about the next step, relative to Treasury's project.

Mr. Allen said that he believes that the Board made some definite decisions about per capita.

Mr. Page addressed the challenge of depicting change over time, that what you want to avoid is showing change in present value amounts over time, because much of that is simply the product of discounting.

Mr. Steinberg said that GAO talks about commitments and contingencies and asked if those are considered in the projections.

Mr. Dacey said that you have to make some basic assumptions, and add some narrative discussions clarify to the readers what is and what is not included. For example, if you have another major New Orleans on top of this, a "mega-disaster," that would be above this.

Mr. Anderson explained that the president's budget assumes that discretionary spending goes down by 2020 and that none of the technical members recommended using it as a baseline.

Mr. Steinberg said that he does not agree with a 100-year projection period because nobody living will be affected by what happens 100 years from now. He said that the projection period should be shorter. He also asked about the definitions of fiscal imbalance and fiscal gap, and asked if the definitions could explain how they relate to a point in time and a period of time.

Mr. Dacey then presented a potential variation of Option C (attached), but adds more information. He explained that this option puts revenue and expense information on two individual programs- Social Security and Medicare Part A-

together and nets them out. He said that all other programs will be competing for the same revenue.

Ms. Parlow said that for the next meeting, staff will provide the various options filled in with as much actual data as possible. In addition, staff will edit the definitions of fiscal imbalance and fiscal gap to explain how they relate to a point in time.

CONCLUSIONS: Staff will continue to develop the exposure draft based on the input received at the meeting. A revised draft as well as additional discussion of issues will be provided for the February meeting.

Attachment- "Option D"

Long-term View - Increase (Decrease) in Long-term Financial Condition

	20X1						20X0		Net Change in Fiscal Condition During the Year	
	Future Resources		Future Responsibilities		Net Resources		Net Resources		PV	% of
	PV Dollars	% of GDP	PV Dollars	% of GDP	PV Dollars	% of GDP	PV	% of		
Social Security	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Medicare - Part A	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Subtotal	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Other Programs										
Medicare - Part B	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Medicare - Part D	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Defense			\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Veterans Benefits			\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Medicaid			\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Other Federal Programs			\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Taxes and Other Revenues	\$ XXX.X	vv v%			\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Subtotal	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%
Fiscal Condition	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$ XXX.X	vv v%	\$	vv v%	\$	vv v%

- **Social Insurance**

Mr. Fontenrose presented two recommendations:

- 1) SI information to include SOSI, SFFAS 17's RSI, a statement of SOSI changes, and an "accrued benefit obligation."
- 2) A general approach for display featuring a highlights table for the MD&A, new line items for the basic statements (with possible notes), a statement of SOSI changes, and current SFFAS 17 RSI.

Mr. Werfel said he had two concerns. First, he observed that the concept of an accrued benefit obligation would encounter some of the same concerns that had been problematic to those supporting the Alternative View. He opined that the notion of an accrued benefit obligation assumes a service has been provided, that something has been earned as the benefit changes. Even though it would not be recorded as a liability, he said it would impact net operating costs.

Second, Mr. Werfel said he found the concept of "maximum transition cost" (MTC) very misleading. He said there was nothing in the law that compels payments to individuals currently in the workforce. He opined that, if the program were shut down tomorrow, there is no obligation or duty to any participant who has not reached the due and payable point. He understood the MTC to be a measure of shutting down the program, liquidating it. He said the MTC seems to imply that there has been an earned benefit that would be owed upon termination of the program. He did not think this was the case, as he understood the program.

Mr. Allen said the staff had attempted to strike a middle ground by proposing information about economic substance while avoiding the accounting question of whether it is a liability or not. This does not raise the question of whether the program could be terminated because no one believes it will be terminated. He said it is not a legal debate but one involving economic assumptions based on what currently is being communicated between the SSA and those people who are making contributions.

Mr. Jackson said an ABO-type measure was a corporate concept reflective of a going concern. For example, it shows what the payout would be if a corporation had to terminate its pension plan, and it connotes a de minimus liability. He said he did not think that that sufficiently reflected the magnitude of the social commitment or social contract regarding tax- or fee-based programs. He said that, unlike future participants, the closed group of participants was a cohort to whom the government had a commitment. He noted that those people were paying into the system and were anticipating that they have earned a right. He said he considered this commitment a social contract rather than something that rises to a true liability measure. Considering the commitment to the closed group and the government as the ultimate going concern, he thought using an ABO measure does feed the notion that the plan may be terminated, that that portion is a greater liability than the commitment to the closed group, which is of greater significance. He said he would not want the information to suggest that the government had made a decision, on any level, in regard to the long-

term continuation of the program. He advised the Board to think about displaying information on the long-term commitment to the closed group population.

Mr. Reid noted that the accrued benefit obligation calculation refers to the portion of scheduled benefits attributable to work already performed, and that there is a controversy over whether any of it is "earned." He said the word "accrued" should be used with care because it connotes a commitment rather than just a calculation. He said that, rather than get into that controversy, he would rather do something that communicates the same information without using that terminology. He suggested terms that would be better, such as benefits "attributed to" or "based on" work performed. He advised using a term that factually represents the circumstances, that does not go beyond the confines of what the statutes say. In addition, he said the Board should be careful about using the term "scheduled benefits" because, again, the statute contains a provision that allows benefits to be reduced if resources are not available.

Mr. Reid objected to putting this information through the net cost calculation. He recommended displaying it on the SOSI; but, within the confines of the SOSI, he thought this information is valuable. He noted that, based on the public hearing, many people want to know what this number is. Mr. Reid said one of the great things about using the SOSI is that it is not limited by the funding mechanism.

Mr. Reid concluded by saying he thought essential information included the accumulated benefits attributed to past work in covered employment as well as a statement of changes in SOSI.

Mr. Steinberg said that he had a slightly different view of essential information than Mr. Reid. He said Mr. Reid was technically correct that benefits are accrued or attributable. He said this only applies to past work in covered employment. He opined that the social insurance problem involved the open group negative net present value, and other numbers added to the SOSI would take attention away from that. He said that if the number were so important it could be in the narrative. In addition, referencing the September minutes, he said the Board had said that the changes in the SOSI was essential information and had identified components to display. He had mentioned four reasons for changes. He said he thought a statement of SOSI changes was needed using those line items. Mr. Steinberg concluded by saying that he thought users are most interested in the SOSI bottom line, that is, the open group net present value and why it changes.

Mr. Dacey said the SOSI changes are important information. He said the actuaries both at Social Security and Medicare analyze changes. He said the Board needed a better understanding of the actuaries' judgments about why they feel their presentation is appropriate and meaningful and what context they would place around them.

With respect to some type of accrued benefit obligation, Mr. Dacey said that, if it were some disclosure support to the SOSI that people find helpful or meaningful, that is fine; but it did not have a place in cost for reasons he had previously stated. He said the

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Board should be careful because that presumes that the Board is assuming policy changes that Congress would make, that this would have a higher priority for payment than other benefits. He said the big concern is over how the standard would be drafted. He said it would be possible to draft it correctly but one would have to be very careful not to convey the wrong message.

Mr. Allen said the calculation is based on what is currently in the law and what is currently being communicated to the citizens. It does not take a position on the relative importance of the amounts.

Mr. Allen said the Board has had feedback over the more narrowly defined issue of liability. He said he had had a lot of positive feedback that the financial statement of the federal government needed to capture the change in economic substance, which is what staff is trying to do while avoiding the liability issue. He said the sustainability report goes a long way to do that, as does the detail of the SOSI, and the statement of changes clearly will help. He did not think there was a question about the value of the information; there was no feedback saying people do not want to see that in the context of the whole government. He said it is valuable information in a broad context. He noted that traditionally a balance sheet captures the over all economic substance of an entity. He mentioned that he had heard a great deal yesterday from economists and others (at the IFAC conference) who say financial statements are not of value because they are not capturing the change in economic value. He said that the staff and the Board are trying to finesse a way to capture the change in economic substance without having to argue the liability issue.

Mr. Allen continued that he believed very much in the value of articulation of financial statements. He noted that GASB had argued for many years about accrual accounting and the modified accrual accounting that governments traditionally used in their fund accounting. GASB had reached a compromise involving statements for the government-wide entity using accrual accounting and statements for funds using modified accrual accounting because of the latter's budgetary focus. The initial response to this GASB "dual perspective" approach was 80-90 percent negative. However, in the end, the simple fact of requiring the modified accrual information with an on-the-face-of-the-statement reconciliation to walk the reader from the modified accrual to the accrual statements carried the day, and now there is tremendous support for that. He said the attempt to off-load the reader to find the information outside the main presentation was not going to be persuasive beyond the Board table. Mr. Allen opined that the numbers need to be linked, albeit not exactly the same; and the closed group number could be used, for example, with other numbers. He said ultimately a vehicle is needed that people can look at and understand by itself and in relation to the whole government. He said he thought the staff proposal did a fairly good job of that, although it would not be his first choice. He understood the concerns expressed by Messrs. Dacey and Werfel and others.

Mr. Dacey said that fiscal sustainability would be very informative by showing net change in fiscal condition within the context of all the revenue and expenses and public policy choices that will have to be made.

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Mr. Steinberg asked if the Board could build on that for the fiscal sustainability standard. He asked whether, if it does not know what the format will be yet, can the Board say these are the elements or attributes of fiscal sustainability and then see what comes out of that.

Mr. Allen answered affirmatively.

Mr. Jackson said the fiscal sustainability report is a long-term look into the future but this report was different. The SI information focuses very narrowly on certain programs. It tries to demonstrate the social commitments the government has made to a constituency of 300 million people in this country, which needs to be reported front and center. He said he viewed that quite differently than the fiscal sustainability report. It is a commitment to those currently eligible to receive benefits.

Mr. Dacey asked what happens if the government is not able to deliver those promises because it has other services that have to be delivered.

Mr. Jackson said that that was why the report is important. He said the government has made these promises now and the constituency expects the government to deliver on them.

Mr. Schumacher said he liked the staff proposal. He said some of the concerns he had were answered in pro forma Display #6 where all the components of the change in the net present values during the period are presented. He said he liked the concept of the ABO, whether “accumulated benefit obligation” or “accrued benefit obligation.” Regarding the balance sheet, he said he still believes that this is a liability as defined in the concepts and should be in the liability section and run through the statement of net cost. However, he said there was room for compromise and the staff proposal moves a lot closer to something the Board can work with where the information is front and center, and can articulate to different pieces of the financial information being presented.

Messrs. Patton and Farrell agreed with Mr. Schumacher that it is a liability. Mr. Farrell said some members were praising numbers in conjunction with having them on the SOSI. He favored having them on the balance sheet and statement of operations in some fashion, perhaps as in the staff’s compromise proposal, because they have to be close to the other numbers. He agreed with Mr. Allen that people are looking at the financial statements and saying all the information is not all there. Having the numbers on the two primary statements – perhaps not in the statements but on the statements – helps the Board get over that hurdle.

Mr. Allen said that commentators who disagreed with the Primary View objected to the absence of future payments by participants. He said this is not a core disagreement. He said, if you look at the Primary View presentation and go back to those comments, he would challenge anybody to come up with – from the comments letters or testimony – that these are not meaningful, valuable measures.

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Mr. Jackson noted that the closed group net present value (NPV) includes future payments. He also noted that there was some history as to why the closed group measure is not explicitly displayed on the SOSI. He said it was important to keep this in mind.

Mr. Jackson objected to using the open group NPV because it includes people who have not been born yet. He was not worried about the people under the age of 15 years but he did not think that, in calculating any kind of commitment to the program's current constituency, that numbers should include the unborn. He strongly endorsed the closed group measure. He said that, if the Board wanted to convey the commitment from a balance sheet perspective, wherever reported, the Board would be constrained, conceptually, to use nothing greater than the closed group measure.

Mr. Allen concluded that the Board's focus was primarily on the sustainability report, and the Social Insurance Project staff should be given the opportunity to work on a few other options. He said he would prefer that the sustainability reporting issue develop further before voting on social insurance accounting and reporting.

CONCLUSION

The Social Insurance Project staff will continue to develop the accounting and reporting options.

- **Steering Committee Meeting**

The Steering Committee meeting was canceled.

Adjournment

The meeting adjourned at 2:45 PM.