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August 25, 2011

Ms. Wendy M. Payne  
Executive Director  
Federal Accounting Standards Advisory Board (FASAB)  
441 G Street, NW, Suite 6814  
Mailstop 6K17V  
Washington, DC 20548

Dear Ms. Payne:

We appreciate the opportunity to respond to the proposed Statement of Federal Financial Accounting Standards, *Revisions to Identifying and Reporting Earmarked Funds: Amending Statement of Federal Financial Accounting Standards 27* – the exposure draft (ED). We support the Board's efforts to improve federal financial reporting of earmarked funds by clarifying the criteria for determining whether a fund should be classified as an earmarked fund and providing further guidance on the reporting requirements.

In the remainder of this letter we provide our responses to the questions posed in the ED and other comments. Where applicable, proposed language revisions have been provided with added text underscored and deleted text ~~struck through~~.

1. The Board is proposing amendments to state explicitly that the source of the "specifically identified revenues or other financing sources" in paragraph 11 of SFFAS 27 must be external to the federal government, and to clarify the distinction between earmarked funds and the general fund. This issue is discussed in paragraphs A11 - A12 of the Basis for Conclusions. The proposed amendment to paragraph 11.1 of SFFAS 27 can be found in paragraph 6 of this exposure draft. Do you agree or disagree with the proposed amendment? Please provide the rationale for your answer.

KPMG Response: We generally agree with the proposed amendment. However, we have the following comments:

- Paragraph 11.1 uses the term "other financing sources" to refer to certain financing sources other than revenue provided by non-federal sources. If it is the Board's intention to use this term consistent with Statement of Federal Financial Accounting Standards (SFFAS) No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, we recommend providing other examples of "other financing sources" from non-federal sources in addition to the example in SFFAS No. 7 of "seigniorage". If it is not the Board's intention to use the term consistent with SFFAS No. 7, we recommend changing it throughout the ED to, for example, "other resources", to avoid confusion.
- We also noted that the placement of the phrase clarifying that the fund is financed by non-federal sources is not consistent between paragraphs 11, 11.1, 13.1 and 13.2. In paragraph 11, the phrase only identifies revenue as the non-federal source of financing; however, the other two paragraphs



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refer to revenue and other financing sources. We recommend paragraph 11 be modified as follow for consistency, taking into consideration other recommended changes presented in other parts of this letter:

“[11.] Funds from dedicated collections are financed by specifically identified revenues and other financing sources, provided to the government by non-federal sources, often supplemented by other financing sources provided by the federal government, ....”

2. The Board believes that funds established to account for pensions, other retirement benefits, other post-employment benefits, and other employee benefits provided to federal employees (civilian and military) should not be reported as earmarked funds and is proposing that such funds should be excluded from the category of earmarked funds. This issue is discussed in the Basis for Conclusions, paragraphs A15 - A16. The proposed amendment to paragraph 18 of SFFAS 27 can be found in paragraph 10 of this exposure draft. Do you agree or disagree with this exclusion? Please provide the rationale for your answer.

KPMG Response: We do not object to excluding these funds from earmarked funds because the required disclosures for pensions, other retirement benefits, other post-employment benefits, and other employee benefits provided to federal employees under SFFAS No. 5, *Accounting for Liabilities of the Federal Government* and SFFAS No. 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates* continue to be retained.

3. The Board is proposing that component entities would have the option to continue to use the existing format of separate lines or columns to display information on earmarked funds on the face of the balance sheet and statement of changes in net position, or to use an alternative format. Some members question the need for component entities to display information on earmarked funds on the face of the balance sheet and statement of changes in net position. The Board is also proposing that the component entity level reporting should be at a sufficient level of detail to support the U.S. government-wide financial statements. The discussion of this issue may be found in the Basis for Conclusions, paragraphs A17 - A20 and the proposed amendments in paragraph 11. Illustrative financial statements may be found in Appendix F.

(a) Do you agree or disagree with the proposal to provide an option for an alternative format for component entity reporting of earmarked funds? Please provide the rationale for your answer.

KPMG Response: We disagree with the proposal to provide options for component entity reporting of earmarked funds. Given the alternatives, we would prefer that the Board adopt the display of information on earmarked funds parenthetically in the narrative describing key line items as the required display. However, see our response to item 3(b) below.

(b) Do you agree or disagree with the view of some of the members that component entities should not be required to display information on earmarked funds on the face of the balance sheet and statement of changes in net position and that disclosure in the notes is sufficient? Please provide the rationale for your answer.



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KPMG Response: We agree that disclosure in the notes is sufficient. We prefer this approach as the footnote already exists. However, consistent with our position in (a) above and the qualitative characteristic of information in financial reports related to comparability discussed in Statement of Federal Financial Accounting Concepts (SFFAC) No. 1, *Objectives of Federal Financial Reporting*, we recommend that the Board adopt specific presentation rather than providing options for presentation.

(c) Do you agree or disagree with the proposal that the component entity level reporting should be in sufficient detail to fully support the government-wide reporting requirements? Please provide the rationale for your answer.

KPMG Response: We agree that the preparers' of the U.S. Government-wide financial statements need sufficient information for the preparation of those financial statements. However, we do not believe that the evaluation of the sufficiency of this information can be done by the preparer and auditor of the component entity's financial statements. We recommend the following revision to the proposed sentence to remind preparers that the information is used by the preparer of the U.S. Government-wide financial statements:

"The information is intended to provide ~~must be in sufficient~~ detail to support reporting requirements for the U.S. Government-wide financial statements described in (see paragraph 29)."

4. The Board proposes to rescind potentially confusing guidance on eliminations for component entities and instead provide that combined or consolidated amounts are permitted and that amounts be labeled accordingly. The discussion of this issue may be found in the Basis for Conclusions, paragraphs A21 - A25 and the proposed amendments in paragraphs 11 - 12. Do you agree or disagree with this proposed amendment? Please provide the rationale for your answer.

KPMG Response: We disagree with the proposal to provide an option to present amounts as combined and we recommend that the financial information related to earmarked funds be presented on a consolidated basis for the following reasons:

- Presenting the components of net position on the balance sheet on a combined basis, as illustrated in option A of Appendix F, means that assets and liabilities would have to be presented on a combined basis in order for the statement to balance. Assume an entity has only two earmarked funds (fund A and fund B) and elects to present the combined earmarked fund information. Fund A provided services to fund B but has not been reimbursed at the balance sheet close so fund A reports the exchange revenue and an accounts receivable balance and fund B reports the cost and an accounts payable balance. Without the elimination entries for intra-entity activities (consolidation), the assets and liabilities on the balance sheet of the component entity will be overstated. SFFAC No. 5, *Definitions of Elements and Basic Recognition Criteria for Accrual-Basis Financial Statements*, paragraph 18, defines an asset as a resource that embodies economic benefits or services that the federal government controls and paragraph 39, defines a liability as a present obligation of the federal government to provide assets or services to another entity at a determinable date, when a specified event occurs, or on demand. The asset



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and liability balances resulting from the example activity above do not meet these definitions because they are intra-entity balances. The asset does not represent an economic benefit to the entity and the liability does not represent an obligation to provide assets or services to another entity.

- We believe that the presentation of combined balances on a consolidated statement will be confusing.

5. The Board proposes to replace the term "earmarked funds" with "funds from dedicated collections." This issue is addressed in the Basis for Conclusions, paragraphs A6 - A8 and the proposed amendments in paragraphs 4 - 5. To facilitate review, Attachment B displays the text of SFFAS 27 with proposed amendments, including the new term. Do you agree or disagree with the Board's proposal to rename "earmarked funds" and make conforming grammatical changes in SFFAS 27? Please provide the rationale for your answer.

KPMG Response: We agree.

6. The following question applies to funds with a combination of (a) revenues and other financing sources that meet the criteria in paragraph 11 of SFFAS 27 ("non-federal") and (b) general fund appropriations ("federal"). The Board proposes that to be classified as an earmarked fund, a fund should be predominantly funded by revenues from non-federal sources or have non-federal revenues supporting the fund that are material to the reporting entity. The Board has also proposed guidance for situations where the proportion of funding sources may change from year to year. This issue is discussed in the Basis for Conclusions, paragraphs A13 - A14. The proposed revised guidance is in paragraph 7. Do you agree or disagree with the proposed guidance on funds with such sources of funding? Please provide the rationale for your answer.

KPMG Response: We generally agree. However, we recommend the following revisions to the proposed amendment to paragraphs 11 and 13 of SFFAS No. 27, taking into consideration other recommended changes presented in other parts of this letter:

"[11.] Funds from dedicated collections are financed by specifically identified revenues, provided to the government by non-federal sources and may be, often supplemented by other financing sources, which remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits or purposes, and must be accounted for separately from the Government's general revenues. The determination of whether a fund should be classified as a fund from dedicated collections is done at the individual fund level. The three required criteria for a fund from dedicated collections are:

1. A statute committing the Federal Government to use specifically identified revenues and/or other financing sources that are originally provided to the federal government by a non-federal source only for designated activities, benefits or purposes;



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2. Explicit authority for the fund to retain revenues and/or other financing sources not used in the current period for future use to finance the designated activities, benefits, or purposes; and
3. A requirement to account for and report on the receipt, use, and retention of the revenues and/or other financing sources that distinguishes the fund from the Government's general revenues.

In certain circumstances, a fund may be financed by a combination of both federal and non-federal sources. Such a fund should be classified as a fund from dedicated collections if the fund meets the above three criteria and

- Its predominant sources of revenue and other financing sources are non-federal sources, or
- its non-federal sources of revenue and other financing sources are material to the reporting entity.

For example, as currently funded, Medicare Parts B and D meet the first three criteria. Medicare Parts B and D's predominant sources of revenue and other financing sources are federal sources. However, Medicare Parts B and D have non-federal revenue and other financing sources that are material to the reporting entity. Therefore, Medicare Parts B and D should be classified as funds from dedicated collections.

[13] **Fund** in this statement's definition of funds from dedicated collections refers to a "fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations." ~~Classification and reporting should be made at the level of an individual fund. A fund should be classified as a "fund from dedicated collections" if it meets the criteria in paragraphs 11.2 and 11.3 and either:~~

- ~~1. its predominant sources of revenue and other financing sources are nonfederal sources meeting the paragraph 11.1 criterion, or~~
- ~~2. it has non-federal sources of revenue and other financing sources meeting the paragraph 11.1 criterion 5a that are material to the reporting entity.~~

~~For example, as currently funded, Medicare Parts B and D do not have nonfederal sources as described in paragraph 11 as their predominant revenue and other financing sources. However, Medicare Parts B and D do have revenue and other financing sources material to the reporting entity that meet the criteria in paragraph 11. Therefore, Medicare Parts B and D should be classified as funds from dedicated collections."~~



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7. The Board is proposing that the amendments to SFFAS 27 have an effective date of periods beginning after September 30, 2011. Do you agree or disagree with this effective date? Please provide the rationale for your answer.

KPMG Response: We agree.

**Other Comments:**

- We recommend the following changes to the proposed amendment to paragraph 11 to be consistent with the proposed amendment to paragraph 11.1, taking into consideration other recommended changes presented in other parts of this letter:

“Funds from dedicated collections are financed by specifically identified revenues, originally provided to the federal government by non-federal sources, often supplemented by other financing sources.”

- We recommend the following change to the proposed amendment to paragraph 11.3, taking into consideration other recommended changes presented in other parts of this letter:

“A requirement to account for and report on the receipt, use, and retention of the revenues and/or other financing sources of ~~that distinguishes~~ the fund separately from the federal government’s general revenues.”

- We recommend the following change to the proposed amendment to paragraph 22:

“...The total net position shown in the note disclosure should agree with the total net position for ~~earmarked~~ funds from dedicated collections shown on the face of the component entity’s basic financial statements.”

- We recommend the following change to the proposed amendment to paragraph 25:

“The total net position of all ~~earmarked~~ funds from dedicated collections shown in the note disclosure should agree with the net position of ~~earmarked~~ funds from dedicated collections shown on the face of the component entity’s Balance Sheet and the Statement of Changes in Net Position.”

- We recommend that paragraphs 15, 16, 17, 27, 28, 29, 31, 32, 33, 34, and footnote 9 of SFFAS No. 27 are updated to replace the term “earmarked funds” with the new term “funds from dedicated collections”.
- We recommend updating the summary section and appendices of SFFAS No. 27 to reflect the proposed changes in this ED.



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If you have questions about our response, please contact Ms. Amanda Nelson at 202-533-5560 or [aenelson@kpmg.com](mailto:aenelson@kpmg.com).

Very truly yours,

**KPMG LLP**