

From: Fleming, William
Sent: Wednesday, September 28, 2011 7:44 PM
To: Payne, Wendolyn M; Parlow, Eileen W
Subject: SEC Comments Earmarked Funds ED (3)

<<SEC Comments Earmarked Funds ED (3).doc>>

Wendy and Eileen

Please find our comments on the Earmarked Document
Thanks,

Bill Fleming

Branch Chief, Financial Reporting and Policy Branch
SEC

Questions for Respondents

Exposure Draft: *Revisions to Identifying and Reporting Earmarked Funds: Amending Statement of Federal Financial Accounting Standards 27.*

Q1. 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.

A. We agree with the proposed guidance. The clarification reinforces the basic intent that funds collected from the public for a designated purpose should be accounted for in a manner that is transparent to the public. Also, stating that earmarked funds are “often” supplemented by other financing sources may not be correct. For clarity, we suggest the following alternative language in paragraph 6:

Dedicated Revenue Funds from dedicated collections are financed by specifically identified revenues; that are provided to the government by non-federal sources; ~~often supplemented by other financing sources;~~ and which remain available over time. The revenues from non-federal sources may be supplemented by other financing sources.

(Note: See response to Q5 for our opinion on the term “Dedicated Revenue Funds” rather than “funds from dedicated collections.”)

Q2. 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.

A. We agree with the proposed guidance. Pension funds, and similar employee benefit funds, are fundamentally different from funds collected from the general public for a stated purpose. In addition, other disclosure requirements exist to communicate the status of pension-type funds to the public.

Q3. 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.

A. We agree that agencies should be given the flexibility to display information on earmarked funds in a manner that best communicates the information to the reader. This is especially true for agencies with very small or very large earmarked funds in comparison to other activities. For example, the SEC is funded almost entirely with earmarked funds, but occasionally receives minor amounts of appropriated funds. The option to disclose these immaterial amounts in the Notes to the Financial Statements improves the overall clarity of the disclosure while simplifying the presentation of the basic financial statements. On the other hand, agencies with relatively small earmarked were faced with reporting the largest portion of Net Position as "Cumulative Results of Operations – Other," contrary to standard practice that "Other" is reserved for immaterial line items.

We believe the proposed flexibility will improve financial reporting.

(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.

A. As noted in the reply to Question 3(a), we believe that the option to present information on earmarked fund in the Notes to the Financial Statements will significantly improve the clarity of disclosures for certain agencies.

(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.

A. We agree that component agency financial information must support government-wide reporting requirements. However, presentation of earmarked disclosures in the Notes to the Financial Statements of an agency does not prevent the roll-up of government-wide information. In addition, as the quality of Federal financial reporting improves, it is hoped that the support for government-wide reporting can rest more heavily on agency trial balances, rather than on highly summarized published

data. This will reduce the expectation that financial disclosures of relatively small, single mission agencies should mirror the complex disclosures needed for government-wide reporting.

Q4. 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.

A. We agree with the flexibility provided by the Exposure Draft. We agree that if an agency presents a disclosure of earmarked funds, this disclosure may be either combined or consolidated. However, if the reporting entity presents columns for earmarked and non-earmarked funds adding up to agency-wide totals, the total column should agree to the principal financial statements to prevent confusion. In this case, a consolidating statement with a single elimination column would be necessary.

Q5. 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.

A. We strongly agree that the term "earmarked funds" should be discontinued, as this term has created excessive confusion due to its similarity to the budgetary term "earmarks." While "Dedicated Collections" is an acceptable alternative, we believe that the term "Dedicated Revenues" would be clearer to those outside the Federal financial community. (Budgetary accounting tends to use the term "collections" while proprietary accounting uses "revenue." Revenue is a more widely understood concept in the private sector.)

Q6. 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.

A. We agree with the proposed language that indicates that the predominant source of funds should be from non-federal sources, and that the agency should be given some flexibility in applying this requirement.

However, we do not agree with the inference in revised paragraph [26] that the reporting of an individual fund as earmarked or not-earmarked could change from year to year. Paragraph [23], item 3 includes the following disclosure requirement:

3. Any change in legislation during or subsequent to the reporting period and before the issuance of the financial statements that significantly changes the purpose of the fund or that redirects a material portion of the accumulated balance.

Earmarked funds are normally driven by legislative requirements for the use of the revenues. The underlying legislative requirements normally remain stable. The reporting entity should be required to review legislative intent, funding sources and other information, identify a fund as either earmarked or not-earmarked in the long-term, and continue with that reporting.

The presentation of a fund as earmarked or non-earmarked should change only if the nature or use of the fund changes as a result of legislative action or other significant events. This change should be treated as a change in accounting. The principle of consistency requires consistent presentation from year to year. For a fund to frequently switch between earmarked and non-earmarked due to relatively minor variations in fund activities would not benefit the user of financial information.

Q7. 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.

A. While we expect to be able to implement the proposed changes quickly, we do not agree with the proposed effective date. An effective date of “periods beginning after September 30, 2011” would require application of these requirements in the first quarter 2012 financial statements due to the Office of Management and Budget in mid January, 2012. Implementation by this date is not feasible. The implementation date selected should allow time for the issuance of the standard by the Board, issuance of preliminary guidance by OMB and Treasury, and careful review of reporting options by agencies.

We recommend that that the effective date be changed to “periods beginning after September 30, 2012, with early implementation permitted.” This will give agencies with numerous and complex earmarked funds adequate time to review disclosure options.