

Statement of
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Chairman
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before the

House Committee on Oversight and Government Reform
Subcommittee on Government Organization, Efficiency and Financial Management

February 16, 2011

Good afternoon, Mr. Chairman and Members of the Subcommittee.

Thank you for the opportunity to testify regarding the recent report of the Federal Accounting Standards Advisory Board (FASAB) Financial Reporting Model Task Force.

I am currently Chairman of the FASAB. FASAB develops federal accounting standards to meet the information needs of citizens, congressional oversight groups, executive agencies, and other users of federal financial information. Accounting and financial reporting standards are essential for public accountability and for an efficient and effective functioning of our democracy.

My comments today represent my personal opinions, not those of the FASAB, which only formally acts after appropriate open due process and formal vote.

FASAB was established in 1990 by the Department of the Treasury (Treasury), the Office of Management and Budget (OMB), and the Government Accountability Office (GAO) following the passage of the Chief Financial Officers Act. FASAB is recognized by the accounting profession – through the American Institute of Certified Public Accountants – as the source of generally accepted accounting principles, or GAAP, for the federal government. For those of you who are less familiar with accounting, GAAP represents the current, accepted accounting rules that are followed to enable a reporting entity to prepare an auditable set of financial statements. To maintain our standing as the GAAP standard setter, we must be independent, have authority within our domain, be adequately resourced, follow due process procedures, and develop comprehensive and consistent principles.

After twenty years of hard work by the federal community, much good financial information is contained within the annual Financial Report of the United States Government. The size and complexity of the federal government requires financial statements rich with information from varying perspectives—such as budgetary, accrual, and prospective. This makes financial statements complex. While they contain most of the information needed to answer key financial questions that citizens, legislators, or agencies have about the federal government, the inherent complexity raises unique challenges in conveying the information. These challenges can not be overcome solely through information requirements and are, therefore, sometimes beyond the

purview of FASAB. For example, the dominant focus on the cash (or near cash) budgetary information for the federal government means users are not made aware of accrual-based financial statements. Public discussions on deficits and debt are extensive while comprehensive measures of financial position and condition are only occasionally discussed. Many users do not have the training or educational resources needed to understand how accrual information can be used to answer questions different than those intended to be addressed through the more often quoted budgetary numbers.

Accrual-based financial statements recognize economic events and transactions when they occur, rather than when resulting cash flows may take place. They are the mainstay of GAAP-based reports for all types of entities in the United States. I will first briefly touch on the value of accrual-based financial statements for state and local governments based on my experience in that arena and then discuss accrual-based federal financial reporting for the federal government.

Accrual Based Financial Statements for States and Local Governments

During the time I chaired the Governmental Accounting Standards Board (GASB), which establishes GAAP for the approximately 80,000 state and local governments in the United States, we completed work on an accrual-based reporting model for state and local governments. It was a long and controversial process and a major change for governments whose focus had been on short-term financial resources. After the model was finalized in 1999 and state and local governments began reporting under that model, a citizen could find answers to key questions such as (1) how much did services cost and who paid the cost; and (2) how much of costs during that year were paid by taxes that year and how much would be paid by future tax payers.

In addition, the accrual-based financial statements resulted in state and local governments accounting for their infrastructure and long-term obligations, and clearly stating their financial position. Many concerns were expressed by state and local government officials regarding recognizing long-term obligations in their balance sheet and what impact that may have on their bond rating. The response from the bond rating community was that the financial position was not nearly as important as the direction the government was heading (what they were doing about their financial position).

Federal Financial Reporting Challenges

Despite twenty years of experience with the CFO Act the full benefits of providing accrual-based federal financial information to legislators, managers, and citizens are yet to be realized. How to integrate and explain key financial information and how to communicate it in a more user friendly manner are issues at the heart of the Reporting Model Project.

We gathered some ideas about the extent of the challenge in presenting federal financial information when we asked citizens directly. They wanted to know first-hand about the fiscal health of the federal government, rather than having to get the information from other sources like the news media. Also, when we presented them with a financial report, they did not understand terms that we hear discussed in the media practically everyday, like “debt held by the public,” and they were not familiar with the organizational structure of the federal government or the missions of the various agencies. But one message was clear. They wanted understandable financial information about the federal government and its agencies.

Some of this challenge may be addressed through educational efforts. The task force recommended electronic, Web-based reporting which could help better deliver financial information to citizens. With Web-based reporting, educational tools can be incorporated into the presentation. Citizens suggested a video presentation with graphics showing trends and explanations of key measures.

Another federal financial reporting challenge is how to apply accrual accounting to some of the unique and complex transactions and circumstances involving the federal government. To illustrate the challenge of how to apply accrual accounting to some of the federal government's resources and obligations to clearly communicate the financial position and results of operations of the federal government I looked to the last "surplus" year--fiscal year 2000. I also chose fiscal year 2000 because accrual accounting, by recording events and transactions as they occur, complements cash flow information and reflects impending fiscal challenges in advance.

The 143-page fiscal year 2000 Financial Report of the United States Government can be used to answer many financial questions. However, one sometimes needs to search and even add or subtract numbers to arrive at answers. I attempted to answer two basic questions—what was the financial position of the federal government and how much did it change during that year. From then Treasury Secretary O'Neill's opening message, it was clearly a good year, particularly on a cash flow basis. Federal debt held by the public had been reduced by \$223 billion. The message also noted an accrual-based surplus of \$46 billion. The Statement of Operations and Changes in Net Position reflected that the net negative position of the federal government had declined but still reflected a \$5.937 trillion negative net position. I also noted in the Management's Discussion and Analysis (MD&A) that the budget (cash and near cash) surplus for the year was \$237 billion.

Despite all the positive information, I noted the management warning on page 13 that "debt held by the public has been reduced by over \$300 billion since 1998; however, total debt subject to the limit has risen by \$152.2 billion over the same period." I also noted on the chart showing federal debt subject to the debt limit that "Intragovernmental Holdings" increased by \$244 billion during fiscal 2000. Intragovernmental holdings increase when dedicated collections from trust funds, such as Social Security and Medicare, are not needed in the current period and are instead loaned to the federal government. As these dedicated collections are combined with general revenues, one could surmise that budgetary and accrual surpluses during fiscal 2000 primarily resulted from trust fund dedicated collections not needed to pay benefits that year. The real financial stress would come in future years as these borrowings are repaid.

To discover when those repayments might occur, I looked further. Looking at the Stewardship Information on page 56 of the 2000 report, I noted the "Present Value of Long-Range Actuarial Projections." When added together they reflect "Benefit Payments in Excess of Contributions and Earmarked Taxes" of \$13.038 trillion. I wondered how much these shortfalls, often called actuarial deficits, had changed during the fiscal year. Since fiscal year 2000 was the first year that social insurance programs were included in Stewardship Information the equivalent amounts for 1999 were not available. Instead, I then read the 2001 financial statements. The amount had increased in 2001 by \$3.993 trillion to \$17.021 trillion, so the assumption is that there was also a fairly large increase in these commitments during fiscal year 2000. These amounts are not reflected on the Balance Sheet or Operating Statement of the federal government, but do impact the financial condition of the federal government. The financial statements included the message

from then Comptroller General David Walker noting the unsustainability of these programs and the need for reform at the “earliest opportunity.”

These comments are not to imply any inappropriateness in the above noted transactions or non-compliance with federal government GAAP. But to note the difficulty that citizens and others may have in understanding these transactions and what numbers on the federal financial statements represent. Even with fiscal year 2000 being a very positive year compared to recent fiscal years, one could be left wondering how did the federal government’s financial condition change during that year.

Because of the many perspectives represented and the challenges of appropriately presenting information regarding social insurance commitments, the federal financial statements have no single bottom-line for annual operating results or financial position. FASAB recently settled on a financial highlights schedule in MD&A to assist users of the reports. The highlights schedule will include key amounts from the individual financial statements including amounts for social insurance commitments and is required in fiscal year 2011.

Progress over the years makes it clear that key federal officials are seeking to inform financial statement readers of the financial condition of the federal government especially with regard to social insurance programs. These efforts resulted in schedules of key amounts in the MD&A of the financial report. Two different examples of ways used to communicate this information are attached as Illustrations 1 and 2. In addition, a Citizens Guide to the Financial Report of the United States Government was issued starting in 2007 to make key financial information available and more understandable to citizens and others.

As FASAB struggled with how to best report on social insurance commitments, it was suggested by some Board members that the long-term sustainability of the entire suite of federal programs was the most important information that could be communicated. Accordingly FASAB started a project in 2007 and the resulting schedule of long-term fiscal projections was included for the first time in the fiscal year 2010 financial statements (see Illustration 3).

The benefit of comprehensive long-term fiscal projections is that they report on what would happen if current policy were continued without change. In addition, information about the reasons for changes in the projections from year to year will be provided. Such projections help inform readers of the magnitude of fiscal challenges facing the nation.

In mid-2008, the FASAB launched a project to study the financial statements, terminology, and methods used to communicate basic federal financial information (the federal reporting model) and determine how to improve the usefulness of federal financial reports. Recognizing that much of the challenge of conveying information is in preparing and delivering the information, FASAB did not constrain its study to the areas accounting standards can influence. Any findings or recommendations beyond FASAB’s purview, will be communicated to the appropriate parties.

FASAB studied the federal financial reporting information needs of citizens and others interested in the financial condition of the federal government (“users”). Following completion of its user needs study in April 2010, the FASAB organized a task force of well-regarded experts to examine the current federal financial reporting model and make actionable recommendations to increase users’ understanding, access, and use of federal financial information while avoiding costly requirements that do not add value.

Members of the task force are:

- Jonathan D. Breul, Executive Director, IBM Center for The Business of Government, and Partner, IBM's Global Business Services, and former Senior Advisor to the Deputy Director for Management in the Office of Management and Budget (OMB)
- Patricia E. Healy, Executive Consultant, CGI, and former Deputy Chief Financial Officer, U.S. Department of Agriculture
- Michael J. Hettinger, Executive Director of Practice Planning and Marketing, Global Public Sector, Grant Thornton LLP, and former staff director of the House Committee on Government Oversight
- John H. Hummel, retired Partner and Federal Segment Leader, KPMG LLP, and Chair, Certificate of Excellence in Accountability Reporting program sponsored by the Association of Government Accountants
- Edward J. Mazur, Senior Advisor for Public Sector Services, Clifton Gunderson, LLP, and the first Controller of the Office of Federal Financial Management, OMB, and former FASAB member
- Marvin Phaup, Director, Federal Budget Reform Initiative, The Pew Charitable Trusts, and former Deputy Assistant Director, Congressional Budget Office
- Al Runnels, Deputy Chief Financial Officer, Department of the Treasury
- Jeffrey C. Steinhoff, Executive Director, KPMG Government Institute, and Managing Director, KPMG LLP, and former Assistant Comptroller General of the United States for Accounting and Information Management and Managing Director for Financial Management and Assurance at the Government Accountability Office
- Sheila A. Weinberg, founder and CEO, the Institute for Truth in Accounting

FASAB is most appreciative of the significant efforts and contributions of the task force. They have presented their recommendations to the Board and spent time answering our questions. Also of great importance is their willingness to continue to provide feedback as the Board moves forward with this project. The two task force members here today will discuss their specific recommendations. Next week, the FASAB will be identifying priorities from among the task forces recommendations and making plans to further improve the reporting model. I will use this opportunity to invite your feedback at any time on this reporting model project. FASAB views members of the legislative branch as key users of federal financial statement information.

I want to thank the Subcommittee on Government Organizations, Efficiency and Financial Management for your interest in improved federal financial reporting. I will be happy to answer questions you may have. I would also like to publicly thank one of your members, Congressman Jim Cooper, for his efforts in the past to help improve federal financial reporting and invite his and your continued input.

Illustration 1: Overall Perspectives Chart

Overall Perspective (in billions of dollars)	2004			2003			\$ Change
	Balance Sheet	Additional Responsibilities	Combined Amounts	Balance Sheet	Additional Responsibilities	Combined Amounts	
ASSETS							
Inventory, cash	\$ 359	\$ -	\$ 359	\$ 372	\$ -	\$ 372	\$ (14)
Property, plant & equipment	653	-	653	658	-	658	(6)
Loans receivable	221	-	221	221	-	221	(0)
Other	165	-	165	154	-	154	11
Total Assets	\$ 1,397	\$ -	\$ 1,397	\$ 1,405	\$ -	\$ 1,405	\$ (8)
LIABILITIES & NET RESPONSIBILITIES							
Social Insurance							
Medicare (Parts A, B, & D) ¹	-	(24,615)	(24,615)	-	(15,006)	(15,006)	(9,609)
Social Security (OASDI)	-	(12,552)	(12,552)	-	(11,742)	(11,742)	(810)
Other (Railroad Retirement)	-	(112)	(112)	-	(110)	(110)	(2)
Subtotal, Social Insurance	-	(37,279)	(37,279)	-	(26,858)	(26,858)	(10,421)
Fed. empl. & veterans pensions/benefits	(4,062)	-	(4,062)	(3,880)	-	(3,880)	(182)
Federal debt held by the public	(4,329)	-	(4,329)	(3,945)	-	(3,945)	(385)
Other liabilities	(716)	-	(716)	(675)	-	(675)	(41)
Other responsibilities	-	(903)	(903)	-	(862)	(862)	(41)
Total Liabilities & Net Responsibilities	\$ (9,107)	\$ (38,182)	\$ (47,289)	\$ (8,500)	\$ (27,720)	\$ (36,220)	\$ (11,070)
BALANCE (Total Assets minus Total Liabilities & Net Responsibilities)	(\$7,710)	(\$38,182)	(\$45,892)	(\$7,094)	(\$27,720)	(\$34,814)	(\$11,078)

¹ Part D's Medicare Prescription Drug & Transitional Assistance Accounts not included in 2003 because both established after fiscal year 2003.
Note: Details may not add to totals due to rounding.

Source: 2004 Financial Report of the U.S. Government

Illustration 2: The Federal Government's Financial Position and Condition 2009

Table 1			
The Federal Government's Financial Position and Condition			
Dollars in Billions	2009	2008	
Gross Cost	\$ (3,735.6)	\$	(3,891.6)
Less: Earned Revenue	\$ 300.9	\$	250.9
Net Cost of Operations	\$ (3,434.7)	\$	(3,640.7)
Less: Taxes and Other Revenue:	\$ 2,198.4	\$	2,661.4
Net Operating Cost¹	\$ (1,236.3)	\$	(1,009.1)
Assets²:			
Cash & Other Monetary Assets	\$ 393.2	\$	424.5
Loans Receivable and Mortgage-Backed Securities, Net	\$ 538.9	\$	253.8
TARP Direct Loans & Equity Investments, Net	\$ 239.7	\$	-
Property, Plant & Equipment, Net	\$ 784.1	\$	737.7
Other Assets	\$ 712.0	\$	558.7
Total Assets	\$ 2,667.9	\$	1,974.7
Liabilities²:			
Federal Debt Held by the Public	\$ (7,582.7)	\$	(5,836.2)
Federal Employee & Veterans Benefits	\$ (5,283.7)	\$	(5,318.9)
Other Liabilities	\$ (1,257.4)	\$	(1,023.1)
Total Liabilities	\$ (14,123.8)	\$	(12,178.2)
Net Position (Assets minus Liabilities)	\$ (11,455.9)	\$	(10,203.5)
Social Insurance Net Expenditures³:			
Social Security (OASDI)	\$ (7,677)	\$	(6,555)
Medicare (Parts A, B, & D)	\$ (38,107)	\$	(36,312)
Other	\$ (94)	\$	(104)
Total Social Insurance Net Expenditures	\$ (45,878)	\$	(42,970)
Social Insurance Net Expenditures as a % of Gross Domestic Product (GDP)⁴			
Social Security (OASDI)	-1.0%		-0.9%
Medicare (Parts A, B, & D)	-4.8%		-4.6%
Other	0.0%		0.0%
Total Net Expenditures as % of GDP	-5.8%		-5.4%

1 Source: Statement of Operations and Change in Net Position. Net Operating Cost includes adjustment for Unmatched Transactions and Balances

2 Source: Balance Sheet

3 Source: Statement of Social Insurance (SOI). Amounts equal estimated present value of projected revenues and expenditures for scheduled benefits over the next 75 years of certain 'Social Insurance' programs (Social Security, Medicare Parts A, B, & D, Railroad Retirement, and Black Lung). Amounts reflect 'Open Group' totals (all current and projected program participants during the 75-year projection period).

4 Social Insurance values as reported in the Statement of Social Insurance. GDP values from the 2009 Social Security and Medicare Trust Fund Reports represent the present value of GDP over the 75 year projection period.

Source: 2009 Financial Report of the U.S. Government

Illustration 3: Illustrative Statement of Sustainability

Long-Term Fiscal Projections for the U.S. Government

Amounts projected to 75 years

	As of XXXX XX, 20XX (Current Year)		As of XXXX XX, 20XX (Prior Year)		Change from Prior Year	
	PV Dollars in trillions	% of the PV of GDP	PV Dollars in trillions	% of the PV of GDP	PV Dollars in trillions	% of the PV of GDP
RECEIPTS						
Medicare	\$ XX.X	X.X%	\$ XX.X	X.X%	\$ X.X	X.X%
Social Security	XX.X	X.X%	XX.X	X.X%	X.X	X.X%
All Other Receipts	XX.X	X.X%	XX.X	X.X%	X.X	X.X%
Total Receipts	\$ XXX.X	X.X%	\$ XX.X	X.X%	\$ X.X	X.X%
NON-INTEREST SPENDING						
Medicare	\$ XX.X	X.X%	\$ XX.X	X.X%	\$ X.X	X.X%
Medicaid	XX.X	X.X%	XX.X	X.X%	X.X	X.X%
Social Security	XX.X	X.X%	XX.X	X.X%	X.X	X.X%
Major Program A	X.X	X.X%	XX.X	X.X%	X.X	X.X%
Major Program B	X.X	X.X%	XX.X	X.X%	X.X	X.X%
Rest of Federal Government**	XX.X	X.X%	XX.X	X.X%	X.X	X.X%
Total Non-Interest Spending	\$ XXX.X	X.X%	\$ XX.X	X.X%	\$ X.X	X.X%
Non-Interest Spending in Excess of Receipts	\$ XX.X	X.X%	\$ XX.X	X.X%	\$ X.X	X.X%

To maintain the current [or date] level of U.S. Treasury debt held by the public to GDP, actions would need to be taken to increase receipts or decrease non-interest spending by a net present value of \$XX.X trillion or X percent of GDP.

Source: Statement of Federal Financial Accounting Standards 36, Comprehensive Long-Term Projections for the U.S. Government

Tom L. Allen - Short Biographical Summary

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| 2006 - Present | Member/Chairman Federal Accounting Standards Advisory Board |
| 2005 - Present | Visiting Professor of Accounting at Weber State University in Ogden, Utah |
| 1994 - 2004 | Member/Chairman Governmental Accounting Standards Board - Financial Accounting Foundation |
| 1983 - 1994 | Elected State Auditor - State of Utah |