

Accounting and Auditing Policy Committee News

The newly formed Accounting and Auditing Policy Committee (AAPC) will hold its first meeting on July 16th from 1:00 to 4:00 pm in Room 4N30 of the GAO Building at 441 G Street, NW. The AAPC will consider a draft charter and operating procedures, means of prioritizing work, and formats for submission of issues.

The meeting will be open to observers. However, due to security requirements and space considerations, we ask that you notify Marian Nicholson at 202 512-7350 if you plan to attend.

Future meetings of the AAPC are scheduled for July 30, September 12, October 9, November 13 and December 11. All meetings are to be held in Room 4N30 of the GAO Building. The AAPC tentatively plans to continue monthly meetings from 1:00 to 4:00 pm on the second Thursday of each month. Any changes to this schedule will be announced in advance.

The AAPC plans to provide an article for inclusion in the **FASAB News** each month. The article will include topics for coming meetings. In addition, Financenet has established a home page for the AAPC. The page is located at:

<http://www.financenet.gov/fed/aapc.htm>

Technical Corrections to SFFAS 6 and SRAS 8 Considered

At the June Board meeting, the Board discussed changes that had been proposed at the May Board meeting to the standards for Federal mission property, plant, and equipment ("Federal mission PP&E") and multi-use heritage assets. The proposed changes affect both

Statement of Federal Financial Accounting Standards No. 6 (SFFAS 6), *Accounting for Property, Plant, and Equipment*, and Statement of Recommended Accounting Standards No. 8 (SRAS 8), *Supplementary Stewardship Reporting*. Any changes under consideration by the Board would be exposed for comment in the same manner that the original standards for PP&E were exposed.

Staff presented proposed changes to the Board in three parts: a) those affecting Federal mission PP&E in both SFFAS 6 and SRAS 8; b) those affecting Federal mission PP&E in only SRAS 8; and c) those affecting multi-use heritage assets in both SFFAS 6 and SRAS 8.

• PROPOSED CHANGES TO FEDERAL MISSION PP&E IN SFFAS 6 AND SRAS 8

In SFFAS 6, Federal mission PP&E is PP&E used to meet a Federal Government mission in which the PP&E used is an integral part of the output of the mission. The Board defined the category as including specific types of PP&E, that is, weapons systems and space exploration equipment, or PP&E that exhibited certain characteristics having to do with use and useful life. The Board specifically identified weapons systems and space exploration equipment as Federal mission PP&E because it did not believe applying depreciation accounting would contribute to measuring the cost of outputs produced, or to assessing operating performance in any given accounting period. The Board believed that these assets were developed, used, and retired in a manner that did not lend itself to a "systematic and rational" assignment of costs to accounting periods (i.e., depreciation accounting) and, ultimately, to outputs.

However, in response to questions from agencies implementing SFFAS 6 regarding the definition and criteria, auditor concerns about agencies' misapplication of the definition, and concerns of some Board members about the type of data to be reported, the Board last month tentatively decided to amend the definition and to reconsider the reporting requirements of Federal mission PP&E. Moreover, some Board members believed that it could be argued that space exploration equipment might not meet the criteria, and should be reclassified as general PP&E.

The Board's primary objective in developing the Federal mission PP&E category had been that this category should exist to provide a means for the Department of Defense (DoD) to report on weapons systems for which depreciation was not meaningful and for which it was difficult to provide accurate historical information. Therefore, in going back to this primary objective and in addressing some Board member concerns that it might not fit the criteria, last month the Board tentatively agreed to drop space exploration equipment from the Federal mission PP&E category (see related article, which follows). It tentatively decided to narrow the definition to include only military weapons systems. As a result, at the June meeting, the Board considered renaming the category from the broader, "Federal mission PP&E," to the narrower "National defense PP&E."

Staff presented revised versions of the standards in SFFAS 6 and SRAS 8 to reflect the new category name of National defense PP&E. The proposed new definition limits the items to two classes of PP&E: 1) weapons systems PP&E used by military departments solely in performance of their military missions, and 2) the Maritime Administration's Naval Defense Reserve Fleet ships. There is a pending Coast Guard request to classify some of its vessels and aircraft as National Defense PP&E. This issue will be discussed at the July Board meeting. If it

is determined that some of the Coast Guard's PP&E qualifies to be included, then a third class of PP&E could be added to the proposed definition.

Moreover, the proposed new definition of National defense PP&E eliminates the "use" and "useful life" characteristics in the former Federal mission PP&E definition. The proposed National defense PP&E definition presents a more functionally aligned category, thus negating the need for the characteristics. Discussion of the "use" and "useful life" characteristics, however, will be presented in the Basis for Conclusion of the proposed new standard.

• ***PROPOSED CHANGES TO FEDERAL MISSION PP&E IN SRAS 8***

In addition to the above changes, the proposed changes to Federal mission PP&E (National defense PP&E) affecting only SRAS 8 relate to the type of information to be reported. The Board proposed that rather than reporting the latest acquisition cost for each major type of equipment for Federal mission PP&E, it would like to examine the possibility of using trend data presented in the Selected Acquisition Report (SAR), a report prepared by DoD for Congress, as the basis for reporting cost trends over a five year period. It believes that the SAR cost data will be more reliable to report than latest acquisition cost data. In addition to reporting cost trend data, the Board proposed that quantities of National defense PP&E would also be reported.

- **PROPOSED CHANGES TO MULTIUSE HERITAGE ASSETS IN SFFAS 6 AND SRAS 8**

SFFAS 6 required special treatment for multi-use heritage assets, those assets that provide reminders of our heritage while being used in day-to-day Government operations unrelated to the assets themselves. The cost of renovating, improving, or reconstructing operating components of heritage assets used in government operations were to be included in general PP&E. Following initial construction, any renovation, improvement or reconstruction costs to facilitate government operations (e.g., installation of communications wiring or redesign of office space) would be capitalized and depreciated over the heritage assets' expected useful life. However, costs of renovating or reconstructing heritage assets that could not be directly associated with operations was to be considered heritage asset costs, not depreciated, and reported as stewardship PP&E.

The Board proposed two major changes to multi-use heritage assets that affect both SFFAS 6 and SRAS 8: 1) to require that multi-use heritage assets be treated as general PP&E, and 2) to clarify the accounting for transfers of heritage assets.

Staff will make the revisions to SFFAS 6 and SRAS 8 proposed by the Board at its June meeting. The Board will review these modified standards at its July meeting. An exposure draft including these proposed modifications is expected in September or October 1997. For further information, contact Rick Wascak, 202-512-7363, email wascakr.fasab@gao.gov.

NASA Chief Financial Officer Addresses Board on SFFAS 6 Issue

As explained in the above article, at the May Board meeting, the Board tentatively decided that based on their proposed narrowing of Federal mission PP&E to National defense PP&E, space exploration equipment should be reclassified as general PP&E. The Board asked that the Chief Financial Officer of the National Aeronautics and Space Administration (NASA), Mr. Arnold G. Holtz, be consulted prior to making this change so as to assess the impact on NASA. As a result, Mr. Holtz asked to address the Board on the issue at the June meeting.

Mr. Holtz believes all assets, not just general PP&E, should be reported on the Federal Government's balance sheet. He believes that depreciation accounting should be applied to all categories of capital assets because the resulting data facilitates comparative assessments of performance, supports the allocation of inter-period costs, and properly reduces the net worth of the Federal Government for related expenses.

Mr. Holtz said that if NASA is redirected to report space exploration equipment as general PP&E rather than Federal Mission PP&E, NASA would have to make significant modifications to its implementation of the standards. As a result, NASA would need a delay in the effective date for implementing the revised standard. He also suggested that FASAB should consider agency testing of proposed standards to confirm, modify, or limit the mandatory application of certain standards.

The Board thanked Mr. Holtz for his presentation. In its discussion following Mr. Holtz's remarks, however, the Board reaffirmed its position that the Federal Government is unique and functions differently than the private sector. As a result, the traditional balance sheet cannot report all of the Federal Government's data, nor does depreciation accounting apply to all Federal Government PP&E.

Internal Use Software

On June 25, the Board published the exposure draft (ED), *Accounting for Internal Use Software*. The ED is being mailed to FASAB's mailing list subscribers. The ED also is available on the Internet, through FASAB's home page:

<http://www.financenet.gov/fasab.htm>

If you are not on FASAB's mailing list and do not have access to the FASAB home page, please contact Marian Nicholson at 202 512-7350 to request a copy of the ED.

The ED defines "internal use software;" distinguishes between the costs of software maintenance, to be expensed when incurred, and capitalizable costs; establishes points when capitalization starts and stops for software under development; and provides for entity-determined capitalization thresholds and amortization periods. Also, the Board notes in the ED that the costs of software modifications to accommodate the year 2000 changes are maintenance costs to be expensed when incurred.

Respondents are requested to address certain specific questions in the ED, as well as to provide any other comments on the ED that they might have. The deadline for comments is September 25, 1995. In addition to mailing your written comments, we ask that you submit your comments electronically. Comments should be e-mailed to comesw.fasab@gao.gov. We would appreciate receiving files in Wordperfect format but can accept ASCII text files.

For further information, contact Rich Fontenrose, 202-512-7358, or email at fontenrosr.fasab@gao.gov.

Management's Discussion and Analysis

In June, the Board discussed three general questions about how to proceed with the project on Management's Discussion and Analysis (MD&A) in light of the 30 comment letters it had

received on the exposure draft.

- What place or role should MD&A have in the overall Federal financial reporting model? For example, should MD&A relate to the financial statements *per se*, or should MD&A also deal with performance measures, internal control, and other information relevant to the objectives of federal financial reporting?
- Should the final document include recommended standards as well as concepts?
- Can the Board specify ways to maximize objectivity in MD&A?

Members expressed different views, as was true of the comment letters. The Board will resolve these and other issues as it deliberates on the specific suggestions from Board members and others. For further information, contact Bob Bramlett, 202-512-7355, email bramlett.fasab@gao.gov.

Update on the Cost of Capital Project

Task force chair, James Blum, his staff, and FASAB project staff (the staff level working group for this project) have been busy laying the groundwork for issues to be considered when the reinstated cost of capital task force review group has its first meeting. Specifically, the staff level working group has:

- requested that the Governmental Accounting Standards Board (GASB) provide information on whether GASB has addressed cost of capital issues and whether there are any state or local governments that include cost of capital in their internal financial reporting or budgeting. The Chairman of GASB has agreed to provide the FASAB with pertinent information;

- designed and forwarded a questionnaire on uses of cost of capital in private sector companies. The Private Sector Council, an organization that assists the federal government in improving its efficiency, productivity, and management through a cooperative sharing of knowledge between the public and the private sectors, has agreed to forward the questionnaire to its members;
- developed a data base on revolving, enterprise, franchise, and other similar types of accounts for which cost of capital could be useful. This preliminary data base covers total capital assets in excess of \$2 Billion;
- contacted and/or reviewed information from foreign governments that include or are attempting to include cost of capital information in their accounting systems, such as New Zealand, the United Kingdom, Sweden, and Canada; and
- received approval from the acting Chief Financial Office of the Bureau of Engraving and Printing to use the Bureau as the first case study of Federal agencies for which the benefits of cost of capital information could be assessed.

After the working group has completed the initial case study of the Bureau of Engraving and Printing, and analyzed the other information gathered, a meeting of the task force to review the initial results of the preliminary stages of the project will be held. The first meeting of the task force will probably occur by late fall, 1997. For further information, contact Lucy Lomax, 202-512-7359, email lomaxm.fasab@gao.gov, or Richard Mayo, 202-512-7356, email mayor.fasab@gao.gov.

Pension Measurement Date

In June, the Board discussed whether

financial statement preparers who apply the provisions of SFFAS 5, *Accounting for Liabilities of the Federal Government*, can use an actuarial valuation as of the beginning of the fiscal year to measure liabilities for employee pensions and postretirement healthcare. Some people advocate using an actuarial valuation as of the beginning of the fiscal year to measure the liability in reports governed by SFFAS 5 as well as in plan reports published pursuant to Public Law (PL) 95-595. Other people believe that measurements for recognizing liabilities in accordance with SFFAS 5 should be as of the end of the reporting period.

Nancy Kichak, Director of the Office of Personnel Management's (OPM) Office of Actuaries, and Mike Virga, OPM's Senior Pension Actuary, discussed the issue with the Board. Ms. Kichak noted that the plan reports called for by PL 95-595 receive scrutiny from congressional staff. Based on past experience, OPM is concerned that any differences between numbers used in Chief Financial Officer (CFO) Act reports and those in the plan report would cause problems and confusion. Therefore, OPM's preference would be to use the beginning of the year number in both reports. Actuaries at the Department of Defense shared this preference.

Board members' opinions on this issue varied. One Board member suggested that a footnote could explain the difference, and asked whether the 95-595 valuation could be prepared sooner. Ms. Kichak indicated that OPM's actuaries had pushed to have the necessary data available sooner, and that they could get 90% of the necessary information in time. However, there was no point in attempting the valuation without the remaining 10% of the needed information. Another Board member agreed that it would be difficult to do a valuation at the end of the period. He also expressed concern about the potential for debates between the auditor and preparer if projections or estimates were used, and suggested that

beginning of the year valuation be specified, perhaps by OMB in its bulletin on Form and Content.

Other Board members said they believed that OPM should use its best estimate of the actual number at year end. This would be consistent with common practice in the private sector.

OPM proposed a compromise, under which the actuarial liability presented in the general purpose (CFO Act) financial statements would be

. . . based on a projection to the end of the year of the results of a beginning-of-year actuarial valuation. This one-year projection will be performed in December following the end of the fiscal year so that it will be possible to take into account most of the major factors that would otherwise be reflected in a full actuarial valuation, such as the actual pay raise and the actual COLA [Cost of Living Allowance]. As a result, this one-year projection should be quite close to what the actual results will be.

The Board agreed that staff would draft guidance calling for measurement at year-end based on a projection, or "roll forward," of the most recent actuarial valuation. The Board will consider the draft guidance at its July meeting. For further information, contact Bob Bramlett, 202-512-7355, email bramlett@fasab.gao.gov.

Volume I of the FASAB Codification Available on the Web

The General Accounting Office (GAO) has posted an electronic version of *Volume I, Original Statements of Federal Financial Accounting Concepts and Standards*, on its home page. The volume can be found at:

<http://www.gao.gov/policy/volume.pdf>

We encourage you to download the PDF file

and use it with Adobe Acrobat on your own computer. The Acrobat software is an excellent tool and permits you to establish links within the document--a quick way to access your favorite standard!

Agenda for July Meeting

The next meeting of the Board is scheduled for Friday, July 25 at 9:00 am in the GAO Building, Room 7C13, 441 G Street, NW. Agenda items include 1) amendments to property, plant, and equipment standards including the U. S. Coast Guard's request for guidance, 2) a draft interpretation on the pension measurement date, 3) social insurance (primarily Medicare), and 4) Management's Discussion and Analysis issues.

**Documents Issued by the Federal Accounting
Standards Advisory Board (FASAB)**

- Concepts:** SFFAC 1 "Objectives of Federal Financial Reporting," September 2, 1993
GPO stock #041-001-00412-2, \$6.00 - Out of Print
- SFFAC 2 "Entity and Display," June 6, 1995
GPO stock #041-001-00456-1, \$3.75
- Standards:** SFFAS 1 "Accounting for Selected Assets and Liabilities," March 30, 1993
GPO stock #041-001-00403-3, \$4.00 - Out of Print
- SFFAS 2 "Accounting for Direct Loans and Loan Guarantees," August 23, 1993
GPO stock #041-001-00416-5, \$6.00
- SFFAS 3 "Accounting for Inventory and Related Property," October 27, 1993
GPO stock #041-001-0415-7, \$3.50 - Out of Print
- SFFAS 4 "Managerial Cost Accounting Concepts and Standards," July 31, 1995
GPO stock #041-001-00457-2, \$7.50
- SFFAS 5 "Accounting for Liabilities of the Federal Government," December 20, 1995
GPO stock #041-001-00463-7, \$5.50
- SFFAS 6 "Accounting for Property, Plant, and Equipment," November 30, 1995
GPO stock #041-001-00462-9, \$6.50
- SFFAS 7 "Accounting for Revenue and Other Financing Sources," May 10, 1996
GPO stock #041-001-00475-1 (includes Implementation Guide), \$18
- SFFAS 8 "Supplementary Stewardship Reporting," June 26, 1996
Promulgation Expected Oct.-Nov. 1997 **
- Exposure Drafts:** "Management's Discussion and Analysis," February 1997 (Written comments due 5/18/97)
- "Governmentwide Supplementary Stewardship Reporting," June 1997
(Written comments due 9/15/97)
- "Accounting for Internal Use Software," June 25, 1997 (Written comments due by 9/25/97)
- Invitation for Views:** "Accounting for the Cost of Capital by Federal Entities," July 1996

Invitations for Views and Exposure Drafts can be obtained free of charge from FASAB at 202-512-7350. Concepts, standards, and exposure drafts can be purchased from GPO at (202) 512-1800 (until out of print) or accessed by Internet at <http://www.financenet.gov/fasab.htm>

** This Statement, approved by the FASAB Principals in June 1996, is still undergoing a "45 continuous session days" review by Congress before it is promulgated by OMB.

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