

FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD
August 13-14, 2003
Room 7C13
441 G Street NW
Washington, DC 20548

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Wednesday, August 13, 2003

Administrative Matters

- **Attendance**

The following members were present: Chairman Mosso, Messrs. Anania, Calder, Kull, Patton, Reid, Schumacher, and Ms. Cohen

The following ex-officio members were present: JoAnne Boutelle, the Department of Defense, and Douglas Holtz-Eakin, the Congressional Budget Office (CBO),

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- **Introduction of new member, Douglas Holtz-Eakin, Director of the Congressional Budget Office (CBO)**

Chairman Mosso welcomed Douglas Holtz-Eakin. Dr. Holtz-Eakin is currently an ex-officio member from CBO and will become a voting member on October 1st in accordance with the new Memorandum of Understanding.

- **Approval of Minutes**

It was noted that the minutes of June 18-19, 2003 were not approved via e-mail – as is customary. The Chairman called for any comments and hearing none indicated that the minutes included in the binders were approved.

Agenda Topics

- **Stewardship Land and Heritage Assets**

Ms. Loughan led the discussion on the Heritage Assets and Stewardship Land project. She explained a draft of Exposure Draft (ED) Heritage Assets and Stewardship Land: Reclassification from Required Supplementary Information had been distributed to Board members following the June meeting. She has incorporated members' comments in the Ballot ED that was included in the August Board binders. Ms. Loughan suggested that if the Board had any additional comments on the Ballot ED that needed to be resolved, staff would like to address the comments during the meeting so the Board could vote on the ED for issuance.

Ms. Loughan suggested that the Board address the one issue raised regarding the effective date for the proposed standard. Ms. Loughan explained that the effective date is drafted as "periods beginning after September 30, 2005." While this date had been agreed to previously, some members prefer to propose an earlier effective date – that is, "periods beginning after September 30, 2004" which is for FY 2005. Ms. Loughan asked the members for their views.

Chairman Mosso noted that the ED did not contain any major new reporting requirements so an early effective date would be reasonable. The Chairman then opened the issue to the Board for discussion. Mr. Patton observed that if there was any slippage in the time-line, the new standard would not be in place before FY 2005 and the Board's practice has been not to issue a standard with an effective date that precedes its issuance or is made effective during the year of issuance. Mr. Mosso noted that if there were slippage, the effective date could be moved back while considering the comments received. Ms. Loughan also explained that additional time (more than the standard 60-day comment period) is being allowed for the comment period as staff was trying to consider the workloads facing the financial management community at year-end. Staff also noted that the ED currently has a question for respondents regarding whether the effective date is reasonable. Mr. Reid noted that

although the required 90-day congressional review period may lengthen the time before the standard is final, he does not believe it would be a huge issue since the document has been made available and the community would be aware of the Board's decisions. The Chairman requested that the Board vote on the issue—the Board voted to propose that the standards become effective for FY 2005 (“periods beginning after September 30 , 2004”).

Mr. Anania suggested that the language pertaining to the Government-wide reporting be included in separate paragraphs or a separate section, versus tucking the differences in the middle of the document. Mr. Anania suggested that this would make the issue easier to understand for the readers. Staff explained that the presentation in the ED, which includes noting the areas that did not apply to the Government-wide reporting, was chosen as SFFAS 24, Selected Standards for the Consolidated Financial Report of the United States Government, stated that all existing and future standards apply to all Federal entities, including the U.S. Government-wide Financial Statement, unless a standard specifically provides otherwise. Ms. Loughan agreed that the format of this could be changed to have a separate section for the Government-wide reporting. The Board agreed to have the document restructured to provide for a separate section for Government-wide reporting.

Ms. Loughan explained that a few comments had been received from Board members prior to the meeting and staff had included those suggested changes for the Board's approval:

- Staff incorporated a question to the respondents that addresses the fact that the ED uses the term “significant” as one Board member suggested that the term may not be clear to readers. Staff stated that the following question had been added:

This exposure draft uses the term “significant” in par. 28 and 44 to describe heritage assets and stewardship land for which an entity should provide the required disclosures. The consensus of the Board was that the preparer should be allowed to exercise professional judgment in determining if the heritage assets and stewardship land are significant. Do you agree? If not, what factors or criteria should be considered to define certain heritage assets and stewardship land as significant?

The Board agreed with adding the new question for respondents.

- Staff incorporated a footnote for the definition of “condition” as included in the current FASAB Codification glossary.
- Staff included an additional paragraph in the Basis for Conclusions that further explained the new reporting requirement for “brief description of the entity's stewardship policies.”

Mr. Patton suggested that the additional paragraph in the Basis for Conclusion did not adequately clarify what the Board is requesting with respect to the description of the stewardship policy. He explained that a definition for “stewardship policy” should be included within the proposed standard. Several board members concurred with Mr. Patton’s suggestion. Staff noted that there currently is no FASAB definition of stewardship policy. Staff also explained that the current literature for FASB and GASB does not address specific items for the stewardship policy and that in developing the proposed standard, staff assumed that stewardship policies would be related to stewardship and management policy. The Board briefly discussed what they believe stewardship policies should address and directed staff to work with counsel on finalizing language for inclusion in the proposed standard.

The Chairman asked the Board if there were any other issues with the ED that the Board may need to discuss or resolve to be in a position to vote. The Board did not have any other comments. The Chairman directed staff to address the two issues raised by the Board (1. Restructure the ED with a separate section for Government-wide reporting requirements and 2. Include a definition for stewardship policy within the proposed standard) and bring back the revised Ballot ED for the Board’s review and approval (on the 2nd day of the Board meeting.)

[The minutes below document the Board’s discussion on the 2nd day of the meeting relative to this topic.)

Ms. Loughan returned to the Board on Thursday morning with a revised draft ED. Ms. Loughan explained that staff had addressed the two issues raised by the Board during the meeting. Specifically, staff explained that to address the definition of stewardship policy, the following language was added to the proposed standard:

Stewardship policies for heritage assets [stewardship land] are the goals and principles the entity established to guide its acquisition, maintenance, use, and disposal of heritage assets consistent with statutory requirements, prohibitions, and limitations governing the entity and the heritage assets [stewardship land]. While not all encompassing, the policies may address preserving and maintaining condition, providing public use or access, and enhancing the heritage assets’ [stewardship land] value over time.

The Board agreed with the additional language and believed that it addressed their concerns.

Ms. Loughan directed the Board’s attention to the new sections of the ED addressing the Government-wide reporting requirements. The Board agreed with the format, but did have some concerns regarding the requirements. Specifically, Mr. Reid suggested that the information about major categories, acquisitions and withdrawals and condition is too detailed for inclusion in the Government-wide report. He added that in aggregating heritage assets and stewardship land information, the different items and uses are so diverse that it is very difficult to summarize and aggregate for the Government-wide financial statement. The Board agreed that it would be best for the disclosure requirements for the U.S. Government-wide financial statement to provide for

a general discussion and direct users to the applicable entities' financial statements for more detailed information on heritage assets and stewardship land. Mr. Patton also suggested that the Basis for Conclusion include language explaining the Board's decision to limit the disclosure requirements for the Government-wide financial statement.

Mr. Kull asked that the Board consider adding a question to respondents in the ED about capitalizing improvements to heritage assets (rather than expensing such improvements). He explained that paragraph 21 of the ED reads:

With the exception of multi-use heritage assets (addressed in par. 24) the cost of acquisition, improvement, reconstruction, or renovation of heritage assets should be recognized on the statement of net cost for the period in which the cost is incurred. The cost should include all costs incurred during the period to bring the item to its current condition (See par. 26 of SFFAS 6 for examples of the costs to be considered).

Mr. Kull explained that it would be consistent to capitalize these types of items that the Board is now proposing to link to the Balance Sheet. The Chairman explained that the scope of the project was limited to the reclassification of the information and that the Board does recognize that this issue (capitalization and measurement) may be a future project of the Board. The Board earlier rejected this suggestion since it would expand the scope of the project. Mr. Kull indicated that the question was exploratory and a means of obtaining feedback from the community, but the Board was firm in its decision to not include the question in the ED, although it did agree with the concern.

CONCLUSION: Ms. Loughan was asked to revise the draft ED before the Board adjourned on Thursday so members could vote on it. However, the Board adjourned early on Thursday prior to staff accomplishing the final revisions. Therefore, staff e-mailed the Ballot ED to Board members for final review and vote. [NOTE: The Board did vote by ballot email to issue the ED *Heritage Assets and Stewardship Land: Reclassification from Required Supplementary Information* and the ED was issued on August 20, 2003.]

- **Earmarked Funds**

Ms. McKinney opened the discussion by reviewing the changes incorporated into the Exposure Draft since the last meeting. The issues that were still unresolved were the note on investments and two additional issues raised by board members: the need for a paragraph addressing government-wide reporting, and the need to align the definitions of "earmarked", "fund" and "earmarked funds".

Board members first considered the footnote to accompany all earmarked fund investments in Treasury securities. The consensus of the Board was to describe the points required to be included in the footnote and then provide the alternative currently in the proposed standard (as modified in response to comments) as an example. Mr. Patton recommended that the points be presented in bullet form.

Ms. McKinney described the government-wide reporting issues raised by John Farrell, who was unable to attend the Board meeting. These issues included the need to have disclosures on the nature of earmarked funds and how the government commits to fund the balances as well as specific requirements for the government-wide statements.

Mr. Anania and Mr. Mosso both suggested that staff could work with Mr. Reid in developing requirements for the government-wide statements. Mr. Reid thought the explanation about the nature of the earmarked funds would be provided under the Note on Significant Accounting Policies. He added that his concern with requirements on earmarked funds for the consolidated statements was that they not be interpreted to require separate presentation for each fund. He stated that the information should be shown in summary form with reference to individual reports.

Ms. McKinney said that another concern of Board members was the structure of the definition provided in the Executive Summary. Mr. Patton in particular expressed the belief that the terms "earmarked" and "fund" should be individually defined before introducing the term "earmarked fund." Ms. McKinney said that the two terms had originally been inserted as footnotes to provide information somewhat incidental to the main definition. At the June Board meeting several Board members stated that they found the footnotes distracting since they contained information relevant to the main definition of "earmarked funds". In response, staff inserted the footnote material into the main body of the text. However, on finding that the material continued to be confusing, staff felt that the definition for "earmarked funds" should stand alone and any additional reference to the term "fund" or "earmarked" be inserted later in the Executive Summary. Mr. Jacobsen asserted that he considered the explanation of earmarked as something other than the "administrative or informal set-asides of appropriated funds for specific purposes" to be significant and believed it should remain in the main body of the text in the first paragraph. Mr. Kull agreed that the majority of people would think of "earmarked" as the budget term for set-asides of appropriated funds. Mr. Mosso asked the Board members for their opinion. Mr. Patton reiterated that he believed that the term fund should also precede the definition of "earmarked funds" in the text. However, the majority of the Board members were satisfied with the term "fund" being defined more technically further along in the text with a minor revision of the remarks referring to "earmarked."

Mr. Anania asked for an explanation of why early implementation was prohibited. Ms. McKinney deferred to Mr. Reid who explained it was to ensure that the accounting treatment was consistent for the consolidation. Mr. Patton said that the explanation should be added to the Basis of Conclusions.

The Board members then discussed several other points. Mr. Anania observed that it would be helpful if the glossary in a new ED indicated whether a word was already in the consolidated glossary, had been defined in a recent ED or standard, or was new to the ED. Mr. Schumacher asked for an explanation of the treatment of earmarked funds in the proposed standard regarding multiple managers of a fund. Mr. Calder observed that the standard did not contain an effective date except in the introduction. He also objected to the wording of paragraphs 41 through 45 in the Basis for Conclusions,

saying that it perpetuated the myth that there are resources available to fund earmarked balances. Mr. Kilpatrick suggested using language based on the note for investment balances.

Mr. Mosso asked staff to aim for a ballot draft on the ED prior to the October meeting.

- **Concepts-Elements**

Mr. Mosso introduced Ms. Penelope Wardlow to discuss the work GASB has done on elements of financial reporting for state and local governments (SLG). Ms. Wardlow is a consultant to GASB, and was the principal staff person involved in developing a draft GASB statement of concepts on elements of financial reporting. The FASAB had been provided with a copy of that draft.

Ms. Wardlow explained that GASB had used the draft, sometimes referred to as “the blue paper,” since 1996 as a working paper to support its deliberations in other projects. Ms. Wardlow said she would explain why the GASB undertook the project, why it took the approach it did, and where the project may be headed. She noted that there was a draft of the paper subsequent to the one that had been provided to the FASAB, but it was quite similar to the version the Board had received. The draft given to the FASAB includes more explanatory material.

Ms. Wardlow explained that GASB was established in 1984 to succeed the National Council on Governmental Accounting under oversight of the Financial Accounting Foundation. The GASB followed precedents set by FASB by starting with a survey of user needs, with a focus on decision usefulness. One of GASB’s first projects led to its first Statement of Concepts, Objectives of Financial Reporting. The GASB intended to follow up with a conceptual project on elements of financial reporting, but it was not added to the agenda as a separate project until 1993. In earlier years, the Board needed to establish itself and deal with basic issues, including defining a new SLG accounting model. These issues assumed a higher priority than the conceptual project on elements. The GASB therefore dealt with conceptual issues to some extent in the context of other projects, but did not immediately pursue a statement of concepts on elements.

The objectives of the elements project were to define key elements of financial reporting, including assets, liabilities, revenues and expenses, as well as related concepts such as “event,” “transaction,” and “basis of accounting.” The purpose was to give a guide to the Board itself in evaluating items that might be candidates for recognition, deciding what might better be disclosed in notes, etc. The goal was to enhance discipline and continuity in the standards setting process and commonality in use of terms by staff, Board members, and eventually the Board’s constituencies.

GASB considered FASB’s definitions and approach to be relevant, but thought that some differences might be needed due to the differences in environment. Among the

significant differences at the time [prior to GASB 34 implementation], was the fact that most state and local governmental entities were reporting by fund, rather than for the entity as a whole. This led to a report with columns for different funds or fund types, as well as two “self balancing account groups” used to report long term debt and general fixed assets. There was, therefore, an understanding that GASB might need to define some elements or terms related to fund accounting that were not needed in the private sector model (e.g., “expenditures”).

GASB did emulate FASB’s approach in that it did not attempt to define terms by seeing how they were being used. Both FASB and GASB tried to define the essential characteristics of each element. GASB also emulated FASB in distinguishing the decision about how to define an element from the decision whether to recognize it and the decision how to measure it. In other words, an item might possess the characteristics necessary to meet the definition of an element, but not possess the characteristics necessary for recognition on the face of the financial statements. In some cases this decision might be influenced by the objectives of a standard, i.e., what the Board was trying to do.

Staff work and Board deliberations on elements began in 1995. The Board tentatively agreed on working definitions for most elements by the end of the first quarter of 1996. At that point, because work on the reporting model project [which led to GASBS 34] was consuming much of the Board’s and staff’s time, the Board decided to put the elements project on hiatus. To avoid losing the benefit of the work that had been done, the Board directed staff to remind the Board of the definitions periodically in the context of deliberations on other projects.

Ms. Wardlow referred to a diagram that categorized events of a governmental unit in a way that became a key part of GASB’s deliberations on its new reporting model:

- I. Internal Events
 - a. Inter-fund activity
 - i. Reciprocal
 - ii. Nonreciprocal
 - b. Allocations (intra-entity or intra-fund)
- II. External Events
 - a. Transactions
 - i. Exchange and exchange-like
 - ii. Nonexchange
 - b. Other external events

The focus on the governmental unit such as a city or state, rather than a fund or fund group, was a new development. The reporting entity issue is relevant to deliberations about elements, because, when defining “asset” and “liability,” the question of “whose” asset or liability it is usually becomes an issue. The GASB tentatively concluded that it would define “asset” and “liability” in terms of a legal entity that can own assets and sue or be sued (rather than in terms of funds). However, this became a controversial point. It may become controversial again when GASB resumes work on its elements project (now scheduled for 2005).

The GASB also decided that it would be important to distinguish internal movements of resources, which would not affect the financial position of the governmental unit as a whole, from external events, which could have such an effect. SLG accounting had not previously made this distinction clearly and consistently. The distinction between exchange and nonexchange transactions became relevant to the GASB’s deliberations on revenue recognition.

The definitions in the “blue paper” have not been formally exposed as a statement of concepts, but many of the ideas influenced the Board’s deliberations and were incorporated in the new reporting model defined in GASBS 33 and GASB 34.

Ms. Wardlow reviewed the draft working definitions of assets, liabilities, and net assets:

Assets are an entity’s rights to goods, services, or cash flows as a result of past transactions or other events.

Liabilities are an entity’s duty to transfer assets or provide services to other entities as a result of past transactions or other events.

Net assets are the residual amount of an entity’s assets, after deducting its liabilities, that are held for the provision of future services.

She noted similarities and differences in definitions used in various countries. The definition shown for assets, which focuses on “rights” instead of “benefits” (as does FASB) is a simplified version of the UK version. Difficult questions of whether to focus on ownership or control arose when defining “asset,” and may well arise again when GASB resumes work on the project. Examples are common (e.g., with infrastructure) where one governmental unit may technically own something, but another entity may maintain it.

Mr. Patton asked whether using the word “rights” precluded the necessity of looking at probability statements. Ms. Wardlow indicated that the GASB had not been very comfortable with the word “probable,” but it might become an issue when the Board resumed work on the project.

Mr. Mosso asked whether the distinction between “exchange” and “nonexchange” signified something different from the distinction between “reciprocal” and “nonreciprocal.” Ms. Wardlow indicated that in practice there was not a difference, but GASB wanted to assure a clear distinction between internal and external events. GASB

wanted to eliminate the term “quasi external transaction,” which had traditionally been used for sale or reimbursement type “inter-fund transactions” that were regarded as similar to external transactions, e.g., between the General Fund and a utility fund.

Mr. Anania asked about the situation in which one wanted to produce internal financial statements for inter-unit transactions: could these not be viewed as exchanges between units? He found it confusing to distinguish the exchange/nonexchange dichotomy from the reciprocal/nonreciprocal dichotomy. He noted that FASAB’s current definition of liability includes the exchange idea.

Mr. Mosso noted that fund accounting [which contributed to GASB’s concern with this distinction] does not play the same role in federal accounting that it does in SLG accounting. Mr. Anania, in turn, noted that GASB’s use of the term “internal” in the chart was arguably different from FASAB’s, [i.e., “funds” in SLG accounting differ from “component reporting entities” in federal accounting].

Ms. Wardlow agreed, noting that in this context she was referring to governmental-type funds that are simply accounting constructs (such as the “General Fund” or a special revenue fund of an SLG entity) that did not stand alone; unlike funds (for example, a utility fund) that can own assets, sue, and be sued, in their own right. “Governmental type” funds are also different, therefore, from federal agencies. The GASB was trying to emphasize the difference in the context of its new reporting model, which is designed to add reports on the SLG entity as a whole to the traditional reports on bits and pieces in the form of funds.

Ms. Cohen noted that traditionally some SLG entities had many funds.

Mr. Patton asked Ms. Wardlow to elaborate on the logic that supports defining elements separate from a reporting model. She said that GASB decided early on to define elements independent of considerations of measurement focus and/or basis of accounting. GASB uses the term “basis of accounting” to refer to **when** one measures something, and the term “measurement focus” to refer to **what** one measures. GASB began discussing the definition of elements when it was not yet certain what the measurement focus/basis of accounting in the new model would be. In fact, the proposed draft definitions are so similar to FASB’s that one could reasonably say that they are accrual basis definitions. The draft definitions are in the context of the governmental unit as a whole. If an item meets the definition of an asset, the governmental unit would decide to what fund it would be assigned. It would not be an asset of a fund that did not have the same measurement focus. For example, a building might be an asset, but it would not be an asset of a governmental fund if such funds do not measure capital assets.

Mr. Anania observed that FASAB’s objectives include the budgetary perspective, and asked how GASB thinks about the budgetary aspect of SLG accounting. Ms. Wardlow noted that GASB has no authority to set budgetary standards. The definition of a budgetary asset or revenue would depend on the governmental unit’s own definition.

Mr. Kull noted that FASAB also has no authority to set budgetary standards.

Ms. Wardlow said that there is budgetary reporting in SLG accounting, in the form of required budget/actual comparison reporting, but it has to be on the budgetary basis. For example, revenue in such a comparison statement would be recognized on the budgetary basis adopted by the particular governmental entity in question.

Ms. Cohen noted that some SLG jurisdictions have requirements for "GAAP-basis budgeting." New York State, for example, does cast its budget on a GAAP basis, but in truth state budgets operate on a modified cash or modified accrual basis. Ms. Wardlow explained that under the former SLG model, an entity converted the GAAP basis operating statement to the budgetary basis, and then compared with the final approved budget. Often there was no difference, because often the budget was adjusted at year-end to conform to actual results. Under the new model, the comparison is actual results with the original adopted budget. This creates a more substantial variance, without any connotation of good or bad: it is just more information. "Here is what was originally adopted, and here is what actually happened." Of course, to have a fair comparison it is still necessary to convert the GAAP-basis actual to the budgetary basis.

Mr. Kull asked how GASB dealt with entities, like federal agencies, that issue reports but also are part of a larger reporting entity. Ms. Wardlow explained that under the current model, there is a distinction between the "primary" government (e.g., a city or state), and component units, which are not the same thing as the term "component unit" is used in the federal model. For example, a state university might be reported in a separate column as a component unit of a state, but not included in the consolidated totals for the state. The same definition of elements would apply in both cases.

Mr. Patton asked whether the asset definition to support GASB's new model would be different from those considered previously. Ms. Wardlow indicated that she was not sure. In its earlier deliberations, GASB had taken the position that concepts were intended to help the Board in the future, and therefore should not be tailored to fit a particular model. Some of the concepts, such as eliminating the term "inter-fund transaction" are already imbedded in the new model.

Mr. Mosso asked about the GASB's schedule. Ms. Wardlow explained that GASB also has done a lot of work on another concepts project, on communications methods. This project developed when some GASB members observed that there was not a well-developed conceptual basis for deciding what information should be reported on the face of the financial statements, what information should be reported in notes, and what as RSI. Recently the Board decided to focus on completing the communications methods project, then return to elements. An exposure draft on communication methods is expected next June with the final in the year following. Thus work on elements might resume around August of 2005.

Mr. Patton asked, "How one can decide what goes on the balance sheet without a definition of asset?"

[The Board adjourned for lunch.]

- **Concepts-Objectives**

Principles-based standards

Mr. Bramlett opened the discussion by noting the recent SEC *Study Pursuant to Section 108(d) of the Sarbanes-Oxley Act of 2002 on the Adoption by the United States Financial Reporting System of a Principles-Based Accounting System*. [The report is available at <http://www.sec.gov/news/studies/principlesbasedstand.htm>.] The report does not directly apply to FASAB, but some of its recommendations for “objectives-oriented standards” and improvements in the conceptual framework may be of interest. One recommendation, that statements of concepts be elevated to the first place in the hierarchy of accounting guidance after the concepts statements are improved, could—if implemented—have such far-reaching implications that it would likely have some impact on FASAB.

Mr. Anania observed that it seems easier to apply a principles-based approach to some topics than to others. Some subject areas, like derivatives, are inherently complex. A general standard for such subjects is invariably met with requests for guidance.

In response to a question, Ms. Wardlow agreed that there was a dilemma. Writing detailed rules into accounting standards often creates problems, but the lack of detailed rules often leads people to ask for them, saying, “just tell us what to do.”

Mr. Anania said his goal would be to write general standards, but provide examples and even detailed criteria when needed to deal with a given topic. The definition of asset is an example: the definition must be supported by more detailed guidance. Ms. Wardlow agreed.

Mr. Mosso recalled that FASAB members had, in a prior discussion, said they perceived FASAB’s standards to be less detailed than FASB’s. Mr. Anania agreed, observing that FASAB’s standards are less voluminous than FASB’s.

Objectives

Mr. Bramlett noted that the Board had requested more background information on internal control reporting and on laws relevant to federal financial management that might be of special interest to FASAB. He reviewed with the Board the background material that had been provided on these topics, starting with the Federal Managers Financial Integrity Act (FMFIA). Mr. Jacobson elaborated on some of the history of reporting on internal control, from the FMFIA to the Sarbanes-Oxley Act.

Mr. Anania asked about the possible implication of the provision of the Sarbanes-Oxley Act calling for the auditor’s attestation regarding internal control. Mr. Bramlett explained that the PCAOB is currently considering the nature of the detailed implementation guidance it should provide about that topic.

Mr. Anania expressed concern that expectations might be too high about what FASAB could or would do in response to the objectives described in SFFAC 1. He asked whether those expectations related to the internal control objective might already be addressed in some other way.

Mr. Calder agreed that there are differing opinions about federal practice and policy regarding reports on internal control. There is a movement toward requiring reports on internal control, and there are disagreements about what the report might say.

Mr. Jacobson noted that even among federal entities required to have audited financial statements, different requirements apply to different entities. For example, when Congress passed the Accountability of Tax Dollars Act of 2002 to extend the requirement for annual audited financial statements to almost all executive branch agencies, it did not apply the FFMIA requirement that applies to CFO Act agencies for reporting on whether financial systems comply with federal systems requirements, accounting standards, and the SGL.

Mr. Patton asked about the objectives of the Board's review. As we review our four objectives, are we to assess whether some other organization has a comparative advantage in looking after those things instead of us?

Mr. Mosso agreed that is where we are headed. In terms of the project plan, we are at the point of evaluating the objectives. They may not need wholesale revision, but the passage of time and changed conditions may suggest some changes.

Mr. Bramlett observed that while preparing the background material, he realized that there had been a significant change since the Board was created which might affect how new members perceived and assessed FASAB's objectives. When the Board was established, a central part of its reason for being was simply to provide a means to bridge the gap between the executive and legislative branches regarding accounting standards. Before FASAB, there had been no arena in which the two branches would work together to reach agreement on applicable standards for audited financial statements. That function remains essential, but it has been accomplished so well that it is now taken for granted. This may free the Board to focus on other, higher-level objectives.

Mr. Anania said his first reaction to reading SFFAC 1 was alarm at the scope of the objectives. On closer reading, he noted that all the objectives include the word "assist" – not saying that financial statements are the only source of comfort regarding each objective. He still has a little concern about overstating the objectives of financial reporting. He wondered about the implications of laws like the Improper Payments Act of 2002: should this information be included in the financial statements now, or only in separate reports to Congress? What responsibility does FASAB have in that regard? Is it the plan that this information be included in the external financial reporting? [OMB Memorandum 03-13, dated May 21, 2003, provides guidance to agencies on reporting

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pursuant to this law. It calls for certain information to be included in the MD&A section of the agency's Performance and Accountability Report.]¹

Mr. Anania said he may be jumping ahead, but he still needs more information about what government actions are being taken that give comfort regarding internal control and how that fits in with what FASAB should be doing with regard to our objective. That is why he wondered what parallel there may be with what might eventually be the requirement under Sarbanes-Oxley.

Mr. Calder said he thinks that is an interesting question, particularly since FASAB recently issued a concepts statement saying that the focus of the Consolidated Financial Report should be on the external reader, the citizen and citizen-intermediary .

Ms. Boutelle noted that DoD's Performance and Accountability Report includes a section on the FMFIA material weaknesses and systems.

Mr. Anania said that he was asking how that fits in with what FASAB is trying to do.

Mr. Mosso said this is a question FASAB needs to pursue. Is someone else addressing an objective adequately? If so, we may want to revise how we present the objective. "Maybe we need to de-emphasize it," Mr. Anania said. "If the objective is not being addressed adequately, or could more rigorously be done with the financial statements," Mr. Mosso continued, "we may want to consider whether an accounting standard could usefully address it."

Mr. Anania said that just saying internal control is an indirect effect is not sufficient.

Mr. Mosso asked what the Board would like for the next meeting? Mr. Anania asked if Board members should provide input regarding the questions from the project plan, which had been distributed to the members.

Mr. Mosso said that might be helpful. Also, staff could prepare a paper that might fill them out.

Mr. Reid suggested a matrix of the objectives lined up with recent developments, over the last ten years or so, with an analysis of how the objectives may have been impacted. Staff could assess whether there is a significant contribution being made as a result of reports that are being filed pursuant to the laws that would tend to downgrade an objective. Maybe the torch has been passed as a result of some law; in which case he would want to take out that objective or in some way revise it accordingly.

¹ "Agencies shall include the reporting requirements of this guidance in the Management Discussion and Analysis section of their Performance and Accountability Report for fiscal years ending on or after September 30, 2004. The annual estimate of erroneous payments reported in the Performance and Accountability Report can be based on data from a year other than the fiscal year the Performance and Accountability Report covers. Progress under the requirements of Section 57 of OMB Circular A-11 shall be reported in the FY 2003 Performance and Accountability Reports." OMB Memo 03-13.

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Ms. Comes suggested that it might be necessary to include some laws, such as FMFIA, that preceded the creation of FASAB. She noted SFFAC 1 was written broadly for federal financial reporting; it was not focused exclusively on what FASAB was trying to accomplish.

Mr. Anania said that the distinction in SFFAC 1 between what FASAB does and what others do might be strengthened. Mr. Mosso agreed that idea could probably be clarified.

Mr. Anania said it would be useful to assess which objectives are being dealt with by which standards. One of the draft standards we are currently working on addresses one objective, while another addresses three.

Mr. Reid said he wanted to avoid conflicting requirements or duplications. At the same time, the objectives should also be guidance, so that we cover what needs to be covered.

Mr. Mosso concluded the discussion on objectives by saying that this kind of analysis might provide a focus for addressing the questions in the project plan.

CONCLUSION: Staff will prepare a paper for discussion at the next meeting. The paper will address or begin to address the areas raised by members such as (1) how standards contribute to meeting the objectives and (2) how other federal financial laws and other requirements may contribute to meeting the objectives.

- **AICPA Rule 203 Review Panel Briefing**

The Rule 203 Review Panel was appointed by the American Institute of CPAs (AICPA) leadership to review the mission and operation of FASAB; evaluate whether the FASAB continues to meet the criteria for standard setting bodies; review the implementation of the revised Memorandum of Understanding under which FASAB exists and the operation of the Appointments Panel; and identify opportunities to strengthen FASAB operations and its standard-setting process. Dr. Gary Previts, Case Western Reserve University and the panel chair, introduced panel members Judith O'Dell, O'Dell Valuation Consulting; Marilyn Pendergast, Urbach, Kahn & Werlin; and Sharon Russell, Alabama Department of Examiners of Public Accounts. The final panel member, Pete Smith of the Private Sector Council, was unable to attend. In addition, AICPA staff members Ian MacKay and Mary Foelster were introduced.

Dr. Previts observed that FASAB not only sets standards for the Federal Government but also for the CPA profession. FASAB's recognition by the profession through the AICPA's ethics rules is the reason for the AICPA being involved in reviewing FASAB's operations. Also, he observed that FASAB standards are being looked at by governments around the world.

Dr. Previts reviewed the five criteria for a Rule 203 body:

- Independence

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- Due Process and Standards
- Domain and Authority
- Human and Financial Resources
- Comprehensiveness and Consistency

The panel has:

- developed questions.
- begun constituent interaction.
- planned for meetings with the Board's sponsors.
- placed notices regarding the effort in the CPA Letter and Journal of Accountancy.

So far, areas of interest raised by the panel continue to include monitoring of independence and constituent representation issues. The Panel chair and members will be meeting with the JFMIP Principals – the Board's sponsors -- in coming months to assess their views about the Board, its processes and resources as related to Rule 203 authority.

The panel members encouraged the Board to contact them if any questions or concerns arose.

Adjournment

The meeting adjourned at 3:00 PM.

Thursday, August 14, 2003

Agenda Topics

- **Fiduciary Activities**

The staff summarized the 11 responses received as of August 11 on the exposure draft *Accounting for Fiduciary Activities*, the comment period for which ended July 31. Staff did not ask the Board for decisions at this meeting, except regarding whether a hearing should be held. Staff indicated that staff responses to the comments would be drafted after receiving input from the Board.

The staff said that the respondents generally agreed with the definition of fiduciary activities. However, one respondent said that the definition didn't adequately segregate federal fiduciary funds.

Several respondents questioned the proposed accounting treatment. One respondent said that the distinction for accounting purposes between assets held "in the name of" the non Federal owner and assets held "in the name of" the Federal entity was not clear because the Federal entity's responsibility appeared to be the same. Another

respondent objected to reporting non Federal assets on a Federal entity's balance sheet.

Mr. Anania said that several responses involve the Board's asset definition and the concept of ownership and whether the Federal entity derives any probable economic benefit from the assets. He said it will be hard to resolve these issues unless the Board resorts to a legal determination, i.e., who owns the asset; and then a question arises whether the legal provisions should always control. He said the Board probably would have to revisit the issue of who owns the asset and who gets the benefit. Mr. Mosso said the Board's current asset definition was merely a working one and that the use of the word "owned" was probably unique to the working definition.

The Board discussed the response from the Interior Department objecting to reporting non Federal assets on the Federal entity's balance sheet. The Board discussed the Interior's legal issues with respect to the ongoing Indian litigation as well as the distinction between managing versus supervising the assets. Mr. Anania said perhaps a clearer distinction would be between managing assets and administering the assets.

Several members discussed the notion of control over the non federal asset as perhaps a better concept rather than ownership.

The Board decided that a public hearing should be held on this exposure draft.

Staff said that several respondents would be contacted over the next several weeks to obtain background on and develop the issues raised.

CONCLUSIONS: Staff will arrange for a public hearing at the October meeting. In addition, staff will begin research on the issues raised in the responses with particular emphasis on how proposed asset definitions align with fiduciary activities (assets).

- **Updating the Rules of Procedure**

The Executive Director explained that the rules of procedure have not been updated to align with the most recent Memorandum of Understanding. This draft would accomplish that update. In addition, structural changes were made to clarify the rules. The objective for the Board's discussion was to provide feedback on the new format and identify any issues. Also, members were asked whether the Statement of Members' Responsibilities should be refreshed concurrently with the revision to the rules. Approval of the rules is not expected until a later meeting.

CONCLUSIONS: Members responded favorably to the structural changes to the rules. Revisions for the next meeting will address the following areas and issues:

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1. Whether a waiver of the usual 10 working day ballot due date could be accommodated. This waiver could provide for a longer or shorter period for voting if warranted.
2. Possible improvements to the description of the voting process – for example, to clarify the effect of a tied vote.
3. Removing from the Statement of Members' Responsibilities any portions that are covered or should be covered in the rules.
4. Providing information regarding the nature and status of ex-officio members.
5. Addressing the conduct of meetings.

Members will consider revised rules at the next meeting.

- **AICPA Task Force on Audit Guidance for the Statement of Social Insurance**

Chairman Mosso explained that Pat McNamee, PwC partner and the task force chairman, had been called away. Walter Fennell, a senior manager at PwC and a member of the task force, made a presentation. Mr. Fennell noted that the objective was to have audit guidance in place by March 31, 2004. He acknowledged that the community was anxious to have the guidance as soon as possible. However, he emphasized that the approach planned by the task force is well grounded in existing audit/attest literature. Thus, the essential elements of the draft Statement of Position can be used as a planning tool sooner than March 31, 2004.

Mr. Fennell's briefing addressed management's responsibilities, auditor's responsibilities and the general factors to be considered in the audit. There was a general discussion regarding the role of the Social Security Trustees, whether an audit had been conducted previously, how the technical review conducted every four years would be weighed, and the reliance on the quality of the process in forming an opinion.

Mr. Fennell indicated that the requirements for the notes to the SOSI have been interpreted in various ways. Some believe the assumptions must be presented in the notes and others do not. He opined that FASAB should consider issuing an interpretation or Technical Bulletin to address disclosure of key assumptions to resolve the ambiguity.

Chairman Mosso thanked Mr. Fennell for the presentation. Mr. Fennell noted that members would each receive a copy of the draft guidance for review.

The Board adjourned for lunch.

- **Social Insurance Liability**

The staff presented a preliminary plan for the Social Security accounting project. Mr. Patton asked why the project is limited to Social Security. The staff responded that Social Security was a high priority and had unique characteristics. Mr. Patton said that the concepts that work for Social Security might not work well for other social insurance programs. Mr. Mosso indicated that he had influenced the plan. He said the sponsors are interested in this subject and the time to address it may be propitious since the Administration is receptive and receptivity is something that vacillates depending on the political appointees. Also, he said that the standard-setting process is under criticism for acting slowly, and a Social Security project may be able to move expeditiously since it is widely known and straightforward.

Mr. Kull said the sponsors wanted to move forward with the Statement of Social Insurance but that they wanted to step back and take a look at the broader question of what is a liability. He said the sponsors have focused not only on this liability or potential liability but on the liability represented by all commitments and contingencies.

Mr. Reid added that the sponsors were thinking in terms of whether there are classes of liabilities. He said the question was whether these kinds of programs fall into the same class of liability as those for which liabilities are currently recorded, or should there be perhaps a stratification of liabilities with certain kinds that historically might have been viewed simply as a commitment showing up as a separate class or some other way arrayed on the balance sheet. But he said it was very clear that the sponsors were looking at a full scope; and, if you were going to prioritize liabilities, you'd take the largest one which is not Social Security but Medicare, which is also the fastest growing. He'd rank that program first. He said he'd agree with both Messrs. Patton and Kull that the scope should be expanded.

Mr. Reid also mentioned with respect to expense recognition that the scope should be expanded to include assumption changes in all actuarially computed liabilities not just the few involved with social insurance. He noted that such assumption changes are distorting the Statement of Net Cost (SNC) in the consolidated report and he'd like to see more than a simple commingling on the SNC. He said something needs to be done with the changes due to assumption changes that have the potential to be greater than the entire SNC. Mr. Reid suggested that in the process of considering the effect of these changes on social insurance the Board could consider how to deal with the effects of all changes in assumptions in those types of liabilities, e.g., a separate presentation on the SNC or, better yet, on another statement. Mr. Reid said this issue is something that could be taken up later in the project. He strongly encouraged the Board not to limit the scope of the project to Social Security but to include all social insurance programs.

Mr. Mosso suggested that the FASB's concept of other comprehensive income is similar to what Mr. Reid was suggesting. Mr. Anania said that the standard-setter normally doesn't preclude the preparer from adding more detail; the preparer generally is free to break out line items where necessary.

Mr. Anania noted that other standard-setting bodies are looking into more than one category of liability. There are “hard” liabilities and “softer” liabilities which are more estimated, future looking liabilities. He said certainly social insurance would fall into the latter category as would environmental clean-up obligations . . . He said the Board may want to pursue whether there’s a basis in the Federal model – even though it may not be embedded in other standard-setting models – for three sections in the right side of balance sheet to accommodate “hard” liabilities, “soft” liabilities, and everything else. He suggested some research regarding the FASAB model and the work in this area by other standard-setters. He noted that the work at FASB in this area didn’t get very far. Mr. Anania said that really soft assets generally don’t get recorded. He said it is desirable to look at assets too and have balanced concepts for the left side and the right side of the balance sheet. Also, he noted that FASB has identified concepts of constructive or equitable obligations that might be useful for FASAB liability projects.

Mr. Patton asked Mr. Anania whether he would be open to the idea of a new element. Mr. Anania said he would but that it would fit somewhere in the range of liabilities. . . He said that perhaps some of the items that will be looked at in FASAB liability projects would be unique to the Federal Government without a private sector parallel.

Mr. Mosso asked the Board to address the scope issue – whether to address one social insurance program at a time or all at once. He said he favored setting standards for one program at a time as a way to accelerate the project. He said that starting with Medicare would be all right with him. Mr. Mosso said he didn’t foresee different notions of liability that would apply to each program but that there could be different recognition points.

Mr. Anania suggested looking at the concepts related to all of the social insurance and then split programs off one at a time after the Board is sure it has looked at all of the conceptual aspects. He said he saw it as perhaps four steps: (1) concepts and definitions, (2) Social Security, (3) Medicare, and (4) all other programs.

Mr. Holtz-Eakin suggested beginning with a look at those things that are common to all social insurance programs. He would look at the definitional issue on both the asset and liability sides. He noted that a liability to the Government is an asset for someone else. He favored looking at the concepts first and then moving to the programs. This would avoid having to back up.

Mr. Calder agreed that basic questions should be answered first and then move on to specific questions.

Staff directed the Board’s attention to Mr. Mosso’s definition of liability contained in his memo to Comes, Bramlett, and Fontenrose dated July 24, 2003. Staff noted that even using this definition the precise line where a commitment became a liability would be hard to determine. Mr. Mosso suggested that the Board try to find the line for each social insurance program. He said that the triggering event is sometimes the most problematic aspect of applying a definition.

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The Board members generally agreed with the staff approach and preliminary list of potential issues that had been identified. The Board agreed that definitions of assets and liabilities should be considered together in this project. The project might be linked with the fiduciary activities project as a vehicle to study assets and liabilities. The staff noted that the working definition of "asset" would be considered with this project to achieve symmetry of language.

CONCLUSIONS: Staff will broaden the project plan to include all social insurance programs in the preliminary work. In addition, work on the "asset" definition will be incorporated.

Adjournment

The meeting adjourned at 2:45 PM