FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD
Minutes
April 23-24, 2003
Room 7C13
441 G Street NW
Washington, DC 20548

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Wednesday, April 23, 2003

Administrative Matters

- **Attendance**

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

The following ex-officio members were present: JoAnne Boutelle, the Department of Defense

- **Approval of Minutes**

It was noted that the minutes of February 12-13, 2003 had been approved via e-mail and that a final copy was provided in the binders.

- **Status of Projects Not on the Agenda**

Ms. Comes provided the status of a number of projects as follows:

1. Statement of Federal Financial Accounting Standards (SFFAS) 25, *Reclassification of Stewardship Responsibilities and Eliminating the Current Services Assessment*, has been submitted to the sponsors for the 90-day review. Issuance would be July 17th absent an objection.

2. The 45-day Congressional review period for SFFAS 23, *Eliminating the Category National Defense Property, Plant, and Equipment*, will conclude on May 8th and the document will be issued shortly thereafter.

3. The interpretation on Intradepartmental Costs has been issued.

4. The exposure draft on Fiduciary Activities was issued April 21st.

Ms. Comes indicated that members would receive copies of the final documents as soon as they are available.

- **Staff Proposal for a New Preamble to the Basis for Conclusions**

Ms. Comes directed the members to a hand out showing the current Financial Accounting Standards Board's and the current Governmental Accounting Standards Board's (GASB) preamble to the basis for conclusions. The Board members agreed to take elements of the GASB preamble and the closing paragraph of the staff proposal. The agreed upon language was:

> This appendix discusses factors considered significant by Board members in reaching the conclusions in this Statement. It includes the reasons for accepting certain approaches and rejecting others. Individual members gave greater weight to some factors than to others. The standards enunciated in this statement---not the material in this appendix---should govern the accounting for specific transactions, events or conditions.

Mr. Calder noted that he found paragraph 184 of Statement of Federal Financial Accounting Standard 5 to be a particularly egregious example of how the basis for conclusions could influence preparers and auditors. Paragraph 184 covers health benefits provided by the Veterans Administration to veterans. Despite changes in the program over time, Mr. Calder noted that individuals point to the language in the basis for conclusions as justification for not recognizing a liability. Mr. Calder sought the

Board's consideration of this issue. The Board members indicated a willingness to take up the issue at a later date.

- **Discussion of the Consolidated Financial Report of the US Government for Fiscal Year 2002**

Chairman Mosso asked Mr. Reid to discuss the Fiscal Year (FY) 2002 Consolidated Financial Report (CFR). Mr. Reid indicated that Treasury is working to issue the CFR earlier but such action depends on how quickly agencies can issue their audited reports. He noted that the FY 2003 CFR will be issued earlier and the FY 2004 CFR will be issued by December 15, 2004.

Mr. Kull mentioned that meetings had already been held with fifty percent of the CFO Act agencies (this normally happens later in the year) and every agency so far has indicated that it would have its FY 2003 reports done by November 15, 2003 with a December 15 fall back. He noted that the discussions have included the IGs and there is a good chance for improvement in FY 2003 and this will help ensure that the deadline of November 15, 2004 is met by agencies.

Mr. Anania commented favorably regarding the Statement of Social Insurance (SOSI) indicating that it looks much like what the standard requires (in contrast to prior years). He added that reducing the detail was helpful, i.e., not including the detail for Black Lung and the RRB.

Chairman Mosso noted that the Comptroller General's opinion criticized the manner of preparation. Mr. Reid opined that there might be a problem when agencies collect money to deposit to Treasury's general account. Agencies in some instances may not be recognizing such collections as revenue.

Mr. Reid noted that the Management's Discussion and Analysis (MD&A) summarized items that don't rise to the level of a liability but are commitments (whatever term one may want to use) in the amount of $31 trillion. He opined that it is important to see these numbers in a summarized way – they are numbers that have been in prior CFRs but not summarized.

Summary of Total Governmental Commitments and Assets
(from page 6 of the Financial Report of the US Government for FY 2002)
Category (In billions of dollars)
Sept.30, 2002

Social insurance commitment	24,149.0
Federal post-retirement liabilities	3,589.4
Federal debt held by the public and accrued interest	3,573.2
Other on-balance sheet liabilities	654.1
Other commitments and contingencies	777.4
Total Governmental obligations	32,743.1
Less balance sheet assets	996.5
Less military equipment (1)	616.0
Total Governmental commitments less Governmental assets (2)	31,130.6

(1)Source: Fiscal Year 2004 Analytical Perspectives, page 37,Defense Fixed Reproducible Capital, Nonfinancial Assets.

(2)The power to tax is not reflected as an asset.

Mr. Farrell indicated that the summary was great. He also mentioned that the Wall Street Journal contained two paragraphs about the CFR focusing on the difference in costs from the budget numbers. Mr. Reid explained that there was a press conference when the CFR was released. Mr. Schumacher asked why the stewardship information appeared immediately after the financial statements and before the footnotes? Mr. Reid explained the stewardship information was not intended by FASAB to be less important than information included on the principal financial statements.

Mr. Patton described the CFR as a compliance document noting that the CFR is 134 pages long. Mr. Reid displayed a prototype 48 page popular report that is highly photographic in content. He explained that this is the first attempt at a popular report and it has not been vetted yet. The challenge is to get the report done in a non-political way. Mr. Reid indicated that he did not know how long it would take to get the prototype report approved. He noted that the focus of the report is “safeguarding America’s future” and the $31 trillion figure is in the report. Mr. Reid finished by noting that the prototype does not follow FASAB standards as it is summarized. Mr. Calder opined that it does follow the standards in a condensed fashion. Mr. Patton asked if Treasury intended to have the prototype report audited? Mr. Reid indicated that an audit was not being considered.

Chairman Mosso thanked Mr. Reid for the briefing.

Agenda Topics

- **Earmarked Funds**

Ms. McKinney noted that the last time earmarked funds were discussed at the December 2002 Board meeting the Board requested that staff use the Fish and Wildlife

Service to illustrate accounting and reporting procedures for earmarked funds. For this meeting, staff developed a preliminary Exposure Draft (ED) as well as illustrations on the Fish and Wildlife Service (F&WS).

The illustrations on the F&WS included ones demonstrating the recommendations of the ED that multiple fund managers report on only their portion of the overall fund. Mr. Anania observed that the ED should note that having multiple managers for one fund was an unusual situation. Several Board members made the point that the ED would need to address the effect on reporting entities that changed the funds on which they report (e.g., by removing them from the balance sheet of one entity and including them on the balance sheet of another entity), including the ramifications on early implementation and comparative statements.

Board members discussed the definition proposed in the ED at some length. Some Board members were concerned with the fact that the term “fund” appeared to be central to the definition of earmarked funds, that it relied on Congress’s use of the term “fund”, that the emphasis should be on the dedication of revenues to support a specific activity and not on the fund, and that the term was not consistent with the ED on Fiduciary Activities. Other Board members noted that the definition hinged on an act of congress requiring that all earmarked revenues be accounted for in funds. They also noted that focusing on revenues as the defining event rather than the fund created significant accounting problems because Congress often establishes various sources of revenue and other financing sources for a particular purpose or program, all of which are accounted for in a fund, not separately. Ms. Comes suggested that reversing the emphasis in the definition to stress the earmarking of revenues might satisfy Board Members objections while preserving as a secondary focus the use of a fund to accomplish the earmarking.

Mr. Calder stated that he found the wording provided by the ED for note disclosure describing the nature of intragovernmental investments to be unsatisfactory. In his opinion it was inaccurate to say that the investments were not an asset to the reporting activity but were a liability to the Treasury. He stated that it did not answer the question of whether or not the investments were an asset or a liability and that some people would consider them a liability. Mr. Mosso agreed it needed to be rewritten.

The Board discussed whether the standard would cover revolving funds. The general consensus was that it should not cover intragovernmental funds. Public enterprise funds are revolving funds used for programs authorized by law to conduct a cycle of business-type operations, primarily with the public. Intergovernmental funds are revolving funds that conduct business-type operations primarily within and between government agencies. Language was suggested to exclude them stating that they primarily conducted business with other government units.

Board Members had an extended discussion on whether the inflows of earmarked revenues and other financing sources should be reported in a footnote to the financial statements or on the face of the reporting entity’s financial statements in line items or columns. Some Board members thought the note disclosure would be satisfactory. Mr.

Patton objected to note disclosure based on his belief that the information in a note disclosure is not as visible. Mr. Reid said he would prefer a separate statement of flows, at least for the bigger funds. Ms. McKinney mentioned that most of the major funds were currently reported as separate columns on the statements of net cost. Ms. Comes suggested that staff work with Board members to develop examples of what they had in mind. Mr. Mosso concurred that staff would work with members to provide examples of alternatives.

The Board also discussed whether reporting entities should be required to list all their earmarked funds. Several Board members stated that it was unnecessary because many of the funds were immaterial to the reporting entity. They suggested that the Board might specify a specific number of funds for which identification and separate disclosure would be required. Others thought that it would be helpful to users to have the reporting entities provide the list of funds. Mr. Kull noted that much of the information of interest to users is not available in the financial statements because the details are lost through aggregation of information.

Board members made several other points during the discussion. Regarding the section on special accountability Mr. Schumacher observed that the ED should state that Congress creates an expectation by its action, not a perception. Several Board members indicated that they wanted a requirement added to the standard that additional note disclosure be provided when Congress reprogrammed money earmarked for a special purpose or program. Ms. Cohen observed that citizens wanted to know whether the balance was actually available for the purpose. Mr. Farrell stated that he would also want to know if Congress enacted legislation changing the purpose of earmarked revenues. Mr. Calder stated that there was no need for a note disclosure on fund assets or liabilities since the Board discussion had done away with the notion of funds as a separate accounting entity. He stated that the Board was only interested in the amounts collected for a certain purpose, such as repairing roads, and how much was spent for that purpose.

Ms. Mosso closed the discussion by stating the next ED would address the Board's concerns.

- **Concepts**

Principle-based Standards

Chairman Mosso began the discussion on the material provided to members regarding the Financial Accounting Standards Board (FASB) regarding "principle-based standards." Mr. Anania opined that using such an approach sounds good but is very hard to do – it depends on the subject and complexity. The level of detail in standards is correlated with complexity. Chairman Mosso noted that in setting FASAB standards the level of detail is debated standard by standard. This allows for tailoring of level of detail to the complexity of the subject. He noted that this tailoring is being done even though we have not used terms like “principles based standards.”

Mr. Patton commented that different interpretations of principle based versus rules based standards have been used. In one sense, all our standards can be considered principle based because they are based on concept statements. The question is how specifically prescriptive or rule based the standards should be.

Mr. Calder suggested that if FASAB avoided exceptions, it would essentially accomplish a principle-based solution. Mr. Schumacher agreed saying that financial engineering has not been a problem in the government as it has been in the private sector. Some members noted that agencies are more likely to engage in financial engineering for budgetary accounting.

Mr. Reid also agreed saying that – for proprietary accounting - agencies just want to know what they’re supposed to do – if they can’t do it, they may try to get around it. Mr. Anania opined that FASAB standards are not very detailed – just about right. Mr. Calder agreed that FASAB standards are more principle-based than rule-based.

The Board adjourned for lunch.

- **Concepts**

<u>Presentation on Reporting Objectives</u>

Ms. Justine Rodriguez, Deputy Associate Director for Economic Policy at OMB, and a member of the Task Force on Objectives for Federal Financial Reporting, recounted some of the research behind the development of SFFAC #1. Robert Anderson, Senior Economist at OMB, joined her to discuss the Stewardship chapter in *Analytical Perspectives,* which reflects an economist’s view of the third Objective.

Ms. Rodriguez observed that when FASAB started, the federal government was not such a happy world for accountants. Accounting then was not much used, and there was rivalry between accounting and budgeting. FASAB has helped to increase the usefulness of and demand for accounting. Now most agency budget directors and many of those who are concerned with performance measures report to CFOs.

FASAB was created to bring together people to identify what could be done to increase the usefulness of accounting and to create a framework for it. The Board pursued two lines of inquiry:

- Who were the actual and potential users of federal accounting, and what did they need to know?

- How was the federal government, as a single, sovereign entity, distinctive from other kinds of entities, and what were the implications of those differences for accounting?

The Board wanted to get a fast start. While the objectives task force was thinking about the framework, task forces were working on a variety of standards, typically starting from existing concepts and standards from FASB and GASB. They developed different concepts and standards only when doing so seemed necessary.

The task force on objectives, headed by Ed Mazur (the first Controller in OMB appointed pursuant to the CFO Act of 1990) included people from other parts of the federal government and from outside the federal government, e.g., Marty Ives. Ms. Rodriguez shared with the Board the paper she wrote to start the task force discussion of objectives, and a summary of the adaptations that *Objectives* made to private sector standards (which had been used by the federal government for several decades). [These papers are available for review at FASAB's office.]

Her papers focused attention on the ways in which the federal government is different from a private firm. For example, a firm would focus on earning profits and accumulating wealth; accounting statements measuring these would be the basis for raising funds from investors and creditors. Government, in contrast, provides services to citizens, using funds raised by its sovereign power. This makes the role of the budget dominant in the federal government..

The task force considered what financial statements might contribute. One possible function of financial statements would be to report on performance, as do financial statements of for-profit entities. This would necessarily be reported in a different fashion than is suitable for for-profit entities, because there is no market price for what government does. In lieu of reporting net income, it would be necessary to report the cost of activities, outputs and outcomes. The Objectives task force also concluded that there was a role for reporting information on assets and liabilities that would help improve the management of those assets and liabilities. The goal was to report not just their value but information to see that they were managed well.

There is a mirror image in the use of financial statements by for-profit and not-for-profit entities, including governments. Some information, including the budget, which is regarded as internal, managerial information in the for-profit sector, becomes vital public information in government. *Objectives* says that, due to the nature of the federal government, it is necessary for accountants to look at the whole continuum between internal and external uses and users. Accountants could and should play a role in making government function better.

The Board looked at the kind of financial information needed in a business environment, and asked what the analogue would be in the federal government. Consideration of such factors led to emphasis on the objective of operating performance, with the goal of reporting the cost of outputs and outcomes, as well as the idea that historical budget data might need to be a part of the audited financial statements.

Objectives noted that financial reporting is not and should not attempt to be the only source of information. Accountants have a relative advantage at some things, however, that make a contribution to the objectives listed: budgetary integrity, operating performance, stewardship, and systems and controls.

The Board clearly recommended as part of the audited financial statements a Statement of Budgetary Resources, and a statement that would be a bridge between budgetary resources and the Statement of Net Cost.

One of FASAB's first standards was on accounting for direct loans and loan guarantees. The budget had recently begun to measure credit programs on an accrual basis designed to recognize the cost "up front." There was a feeling that this was the only way that made sense in the budget, but it required new estimates. There was a strong feeling in the budget community that accountants should audit those data and make sure that the measures of the cost of credit programs were sound.

The Federal Credit Reform Act called for a study to assess whether federal insurance programs should be budgeted for in the same way. "Risk assumed" is a name for a credit-reform like measure for insurance programs, especially deposit insurance and pension insurance. Use of that measure has never been enacted for the budget because it is very difficult to measure. Depending on economic conditions, such programs can be subject to a very small but real risk of catastrophic losses. OMB has made estimates of that sort, but is nervous about using them for budgetary purposes. One idea was to let agencies try to make these estimates for disclosure in financial reports. This would provide information, and eventually perhaps greater assurance about what should be recognized in the budget.

Federal employers are already charged for their share of some retiree benefits on an accrual basis; and the Administration has proposed legislation to charge for all such benefits. Similar issues may arise regarding hazardous substances. Many agencies are beginning to do cost accounting, which can provide a background for budgetary estimates. In these ways, accounting can be supportive of budgetary integrity.

The operating performance objective requires an attempt to match cost with the provision of services to the public. This objective led to the Statement of Net Cost. Agencies now report cost broken down by strategic goals, by organization, and budget function. They report actual performance against measures targeted at the beginning of each year. Increasingly in the managerial system, we see analysis of unit cost, marginal cost and so forth.

Mr. Patton said he was trying to see what were the different perspectives on the balance sheet under the operating performance and stewardship objectives. Ms. Rodriguez said there had been a lot of talk about whether the government manages assets and liabilities well. The information called for in objective 2 c was intended to encourage agencies to manage assets and liabilities better. In objective 3, the values on the government-wide balance sheet were the first step in assessing the fiscal condition of the government as a whole and its ability to sustain services into the future.

Mr. Anania said that the objectives stated in SFFAC 1 are very broad. He wonders whether what FASAB is doing matches the objectives. He believes several areas in SFFAC 1 have not been touched. He wonders whether we should see the objectives the same today as when they were formed or should we reassess the objectives versus expectations and our delivery? Would this Board today set the same objectives, if we were doing it in 2003?

Ms. Rodriguez said that is a complicated issue. Is the information needed today? What do accountants contribute to the information that is needed? What are the priorities? She sees potential value in sharpening the objectives, but danger in cutting out too much. Some of the nontraditional parts are not for FASAB to set a standard "for," but to shape standards in "compatibility with." The most obvious example is cost and performance measures. Another example is the idea of including budgetary execution data in your thoughts about what is being reported.

Mr. Anania said that the Board could say, "here is our project," then say "these are the objectives we are dealing with." The other way would be to review the project plan in light of the objectives to see whether we are dealing with as many as we can. Some objectives throw up red flags, for example:

- internal control,
- 2 c "efficiency and effectiveness"
- concern with internal reporting as well as external.

Ms. Rodriguez said that regarding systems and controls, she did not have knowledge to say whether or not that was being done and done well elsewhere, e.g., JFMIP. Others can say better than she whether we should drop the objective or whether it serves a purpose. Regarding management of assets and liabilities, the Board has provided standards for relevant information. There is a lot of that in inventory, credit, deferred maintenance and condition reporting. Perhaps the concept could be framed better, or perhaps different data are needed. With regard to "internal" cost accounting and the Statement of Net Cost, SFFAS #4 envisioned that the full cost of outputs produced by a "responsibility segment" would aggregate to the lines for that segment in the Statement of Net Cost. This is part of the process of assuring that all the costs associated with the segment will be reported. The details may one day be available in "drill down" mode from electronic financial statements. This does not restrict agencies from other uses of cost accounting in other formats.

Mr. Anania questioned whether SFFAC 1 suggests that the Board relies on OMB and GAO for the details needed for internal reporting. Ms. Rodriguez said she thought not, but OMB and Treasury define the format of reporting. Mr. Reid said he thought OMB and Treasury were moving away from defining the format of reporting and that this would soon be obsolete. The objective for 3-day closing was to have data available on a real time basis.

Mr. Kull, referring to Mr. Anania's earlier question, "whether we should see the objectives the same today as when they were formed?" said that in his opinion the answer is "no." The way we operate now is not the way the Government operated 10 years ago. The Administration is trying to drive real-time financial management and affect current operations, understand what is driving the result, and make changes as necessary. That is one level of information about performance, but managers also need to know how much money they can spend. Those are radically different decisions, based on different information systems.

Mr. Anania said "we have said we want to go down a dual path, working on concepts and on standards." He agrees with that, but to do so, he believes we need to revisit the objectives. We need to weigh the objectives against what we have done and what we expect to do, and see whether there is an expectations gap.

Mr. Robert Anderson discussed the chapter on "Stewardship" from the *Analytical Perspectives* volume of the President's Budget. He said that the first table, based on economic data, showed a large net liability, but noted that it did not include the Government's largest asset: the power to tax. Much of the chapter is devoted to long run budget projections, which show that we are on an unsustainable path. The chapter also includes information on national wealth and social indicators. He called attention to chart 3.8 (shown below), which shows how the various assets, liabilities, resources and claims fit together.

Chart 3-8. A Balance Sheet Presentation for The Federal Government

Assets/Resources		Liabilities/Responsibilities
Federal Assets Financial Assets Monetary Assets Mortgages and Other Loans Other Financial Assets Less Expected Loan Losses Physical Assets Fixed Reproducible Capital Defense Nondefense Inventories Non-reproducible Capital Land Mineral Rights	**Federal Governmental Assets and Liabilities (Table 3-1)**	**Federal Liabilities** Financial Liabilities Debt Held by the Public Miscellaneous Guarantees and Insurance Deposit Insurance Pension Benefit Guarantees Loan Guarantees Other Insurance Federal Retiree Pensions and Health Insurance Liabilities Net Balance
Resources/Receipts Projected Receipts	**Long-Run Federal Budget Projections (Table 3-2)** **Actuarial Deficiencies in Social Security and Medicare (Table 3-3)**	**Responsibilities/Outlays** Projected Outlays Surplus/Deficit 75-Year Actuarial Deficiencies in Social Security and Medicare
National Assets/Resources Federally Owned Physical Assets State & Local Physical Assets Federal Contribution Privately Owned Physical Assets Education Capital Federal Contribution R&D Capital Federal Contribution	**National Wealth (Table 3-4)** **Social Indicators (Table 3-5)**	**National Needs/Conditions** Indicators of economic, social, educational, and environmental conditions

Mr. Mosso noted that the top two boxes on the chart correspond to the balance sheet, and that FASAB has standards that deal with pieces of the other boxes. Mr. Patton observed that natural resources are in the upper section of the chart; he asked whether this implied they are or should be recognized on the balance sheet? Mr. Anderson said that data on federally-owned resources were presented. He noted that the data were derived from economic sources, which might not be suitable for recognition in audited financial statements. BEA has its own estimate of fixed reproducible capital. OMB uses BEA's method for measuring federal physical capital, but OMB makes its own estimates.

Mr. Mosso asked whether BEA had an estimate of national wealth. Mr. Anderson said you could get national wealth from their tables, with some omissions. They have estimates of the national stock of reproducible capital for the entire economy and of inventory (except for the federal sector), but not land or natural resources.

Mr. Patton asked who might read table 3-1 (Federal Governmental Assets and Liabilities from 1960 to 2002 in 2002 dollars) and what they do with it? Mr. Anderson said he assumed it would be the same group that read the *Analytical Perspectives*: staff at GAO, OMB and Congress, some members of the press, and various groups interested in public policy. Ross Perot used it at one point, and it surfaced in his campaign.

Mr. Mosso asked Ms. Rodriguez to elaborate on the relationship between the national economy, wealth, and welfare and the Government's financial reporting. Ms. Rodriguez responded by referring to the table, at the top of which are the assets owned by the federal government as a result of past operations. Reading down the column, at one step removed, one finds information about expected future receipts, and below that information about the economy that will generate those future receipts. In the other column one finds reported the liabilities owed by the Government as a result of past operations, followed by a forecast of what we will have to spend to sustain current services, followed by some economic and social indicators that indicate something about the possible demand for future services.

Mr. Anderson distributed a chart that showed how OMB's long-range deficit projections had varied over time as a percent of GDP. Despite these variations, they all showed a similar pattern with eventually larger and larger deficits. Ms. Rodriguez noted that in any one budget, alternative scenarios based on different assumptions are presented.

Mr. Mosso asked whether Treasury was trying to put some of the lower-right-hand box (i.e., indicators of economic, social, educational, and environmental conditions) in OMB's Chart 3-8 in MD&A. Mr. Reid said to some extent yes, Treasury was trying to show the big picture.

Mr. Kull said that the assets have little relation to the liabilities. Mr. Anania agreed, saying the assets don't generate the revenues to pay the liabilities. Mr. Kull said we can't look at the Government like a business. The real asset we have is the projected receipts, and the question becomes "how much is the taxpayer willing to bear." We need financial information to run the Government, but these are different kinds of questions.

Ms Rodriguez suggested that the Stewardship chapter had some influence on the attempts to reduce deficits. It showed not just the liability we had already incurred, but that there is no easy way out because the Government is large enough to affect the overall national economy. When we expected deficits to continue, national wealth was growing more slowly as a result. Although not relevant to individual agencies, having the information for the Government as a whole helps people understand what is worsening our condition, and what changes need to be made to programs or to the economy to be able to continue.

Mr. Anania observed that much of the stewardship objective is focused on the CFR level. Ms. Rodriguez noted that agencies have to report whatever will be aggregated. The concept of "financial position" may be problematic for agencies. Mr. Kull said that individual agencies are extremely important, and noted you can't manage for economy and efficiency based on appropriations.

Ms. Rodriguez concluded by saying that expertise in accounting needs to be linked to other disciplines to illuminate for the federal government issues that might be resolved largely by accounting alone for a private firm.

Mr. Farrell asked, "if we are trying to show the results, why isn't the Board of Directors [the Congress] getting the message?" Mr. Anderson suggested that the message was known, but solutions need to work through the political process. Also, the situation has deteriorated, and it may take time for that to sink in.

Ms. Rodriguez noted that a future Administration could decide to eliminate the Stewardship chapter from *Analytical Perspectives*. There is no legal requirement for it. She noted that the real test of financial condition is the comparison of total future receipts and expenses over the long term under a range of assumptions, not projections for any one program.

- **Natural Resources**

Mr. Wascak began the discussion noting that at the last Board meeting staff was asked to bring back a draft skeletal exposure draft (ED) on the proposed oil and gas standards. He also noted that based on staff's research of the data available on federal oil & gas resources, staff concluded that the oil & gas resources meet FASAB's working definition of an "asset." However, the resources did not meet the criteria for recognition because the resources cannot be reliably measured. Therefore, the draft ED will concentrate on the collections of rents, bonuses, and royalties; the distribution of those collections, and reporting of other quantifiable non-financial information. Staff noted that the reporting would most likely be in "required supplemental information" (RSI). Staff also noted that it would be conducting further research in the areas of collections and distribution of collections to explore current Federal practices. That is, staff would document the flow of collections and distributions within various entities and compare those practices with existing standards before proposing new guidance, where necessary.

Mr. Reid asked if staff had considered disclosing some quantifiable non-financial information in the footnotes. Mr. Wascak responded that staff had not considered disclosing information in the notes. Mr. Mosso suggested that staff research the possibilities of recommending that certain quantifiable information be disclosed in the footnotes. Mr. Farrell noted that the Heritage Assets project is suggesting disclosure of non-financial information in notes as opposed to RSI.

Mr. Calder asked if there were any specific issues relating to the collections and distributions, since there is guidance already in place that deal with those two areas. Mr. Wascak noted that there might be some consistency issues with how collections and disbursements are reported on the Statement of Custodial Activities and the Statement of Net Costs. Mr. Reid asked if collections are reported on a cash basis; and how would the revenue be reported if cash is received upfront on a 10-year lease? Ms. Valentine noted that rental revenue is collected during the lease term until the lessee starts to extract the resource; at that time the rental payments cease and royalty payments begin. The royalties are based on the amount of oil and gas resources extracted. Mr. Farrell asked exactly what are “bonuses” and how are they currently recognized. Staff explained that “bonuses” are paid by the potential lessees at the time they submit their bids. However, only the winning bid’s bonus is retained by the government. Mr. Anania stated the issue of how to recognize the bonuses should be addressed (i.e., should the bonuses be recognized on a cash basis or amortized over the lease term). He also stated that the Board should consider the terms in which the bonus payment is received. For example, if the lessee never “taps” into a resource and only ends up with a “dry hole” is the bonus returned to the lessee. Staff noted that the government would still retain the initial bonus payment. Mr. Anania said that since the bonus payment is not dependent on the future production of the resource, that may be an argument to recognize the bonus at the time it is received as opposed to amortizing the payment.

Mr. Mosso asked staff to research the possibility of recognizing the future royalties revenue stream as an asset at the time the lease is granted. Mr. Farrell noted that the Board will need to address the timing of when collections are recognized. Mr. Anania suggested that staff’s assertion in the draft skeletal exposure draft that while oil and gas resources meet the definition of an asset, yet do not meet the recognition criteria of an asset, should be further developed.

Mr. Patton asked staff how they decided that oil and gas resources did not meet the recognition criteria of an asset (i.e., what attribute is it that can not be measured). Was it the market value of the oil & gas resources still in the ground? Staff replied that the market value of the oil & gas resources still in the ground is not measurable. Mr. Patton stated that just because you cannot measure the market value of something, does not mean it is not measurable. He said you have to determine what attribute you want to measure. He further stated that the Balance Sheet is not the "Statement of Market Value" and to act as if the value is zero is a mistake, even given the fact that the value may be subjective. Mr. Patton suggested that the Board may want to measure some sort of cost basis as opposed to not recognizing a resource of the government.

Mr. Anania pointed out that there are significant differences between the operations of oil & gas resources of private entities and those of the federal government. He said that private entities normally have a cost basis for the acquisition of its resources. Ms. Comes pointed out that it might be misleading if we capitalize the cost of "preparing for a lease sale" as if it represented the cost of the "oil & gas resources." She said this would not be a relevant measure of the vast oil & gas resources that are under the control of the federal government. She also asked if the Board was looking to take a different approach to reporting assets as is done in the Analytical Perspectives' Balance Sheet where "national wealth" measures are the goal.

Mr. Schumacher asked staff if there are estimates available on the government's oil & gas resources. Mr. Wascak explained that the federal government performs geological and engineering analyses every five years on proved and unproved active fields as well as the assessment of inactive areas every five years. Mr. Calder stated that the Board already has a model for reporting non-financial information with Stewardship Land and Heritage Assets. He further suggested that this type of information could be disclosed. Mr. Patton made the point that these types of discussion get at the core of FASAB's reporting objectives. He added that the Board will need to decide what the nature of the Balance Sheet is and what type of "things" belong there. Mr. Patton further stated that getting a number on the Balance Sheet for these resources is very important, especially from an accountability standpoint. He also said that putting a number on the Balance Sheet increases the relevance of the statement compared to acting as if the number is zero.

Mr. Mosso mentioned the amount noted on the Analytical Perspectives in the 2003 Budget for Natural Resources. He stated that based on discussions with budget analysts at OMB, the amount is based on studies performed over twenty years ago and then rolled forward annually based on indexes. He also asked staff to further research the validity of the calculations. Mr. Patton made the comparison to FASB's contingent liability requirement to recognize the minimum number when only a liability range is available. He further reiterated that a minimum asset dollar amount recognized on the Balance Sheet is better than no dollar value, which would be misleading. Mr. Reid asked if it were possible for staff to compare the initial resource assessments to the actual resources extracted. He said that if the initial assessments prove to be adequate compared to the actual extractions, then the initial assessments could be recognized as an asset on the Balance Sheet using a net present value calculation. Mr. Farrell made the point that if this type of asset is recognized, then annually your net revenue for the lease would be zero because as you make collections they will be offset by the amortization of the asset recognized. Mr. Reid asked if the net zero effect is justification enough not to recognize the resource on the Balance Sheet?

Ms. Cohen asked staff to take a look at how natural resources are recognized in the other countries that have significant natural resources. Ms. Cohen also suggested that staff take a look at the state models (i.e., those states, such as Alaska, that have state-owned oil and gas reserves).

Mr. Anania noted that given the structure of the federal oil and gas resource activities it would be a "stretch" to recognize any amount on the Balance Sheet for value of a prospective lease sale, primarily because of the timing of the assessments (every five years) and the lack of existing comparable accounting guidance or practice.

Mr. Kull asked why these resources should be recognized on the Balance Sheet? He asked if it is because the Board is trying to record the future economic value of the resources to the federal government? He also asked if the Board views these resources as a potential revenue stream or as resources of the citizenry that are under the stewardship of the federal government. He added that the Board seems to be viewing this resource in the traditional business construct, with an asset on the Balance Sheet. Mr. Mosso noted that the point behind reporting these resources on the Balance Sheet is "accountability". The comparison was made between national defense property, plant & equipment (PP&E) and federal natural resources. Mr. Patton stated that federal land is held for the purpose of advancing the objectives of the country and there is some sort of future political, economic, or social benefit associated with the land and therefore it is an asset. Thus, there are some measurable features to that asset (i.e., quantity, cost, or market value). He also noted that market value may not be the best measure of these assets on the Balance Sheet.

Ms. Comes asked Mr. Patton if a line item on the Balance Sheet with no dollar value and a footnote reference would be an acceptable method of Balance Sheet recognition? Mr. Patton agreed that recognition on the balance sheet with no dollar amount would be preferable to excluding the item from the balance sheet altogether.

Mr. Mosso asked staff to continue their research on current reporting practices as well as options for measuring the oil & gas resources and come back to the Board for discussion. Mr. Anania also asked for some type of average lease value; comparing total potential lease areas to actual leased area and the value received.

Mr. Patton asked that staff address the minority comments noted in the Discussion Paper. Mr. Farrell asked staff to clarify the definitions used in the ED.

Asset Definition

Ms. Comes asked the Board whether or not they had any comments on the various asset definitions noted in the table of definitions provided in the meeting materals. Mr. Anania asked why FASAB's working definition of an asset did not mention the notion of "service potential" as noted in some of the other definitions. Ms. Comes noted that the notion of "service potential" is embodied in the definitions of PP&E and inventory and the verbiage "probable economic benefit" includes the provision of service. Mr. Patton questioned the use of the word "owned" in FASAB's working definition of an asset. Mr.

Farrell commented on the use of the phrase “results of past transactions and events” in IFAC and FASB’s definitions.

Mr. Patton’s suggested the following definition.

> (A) *Definition*: Federal entity “Assets” are resources (rights to probable inflows of goods, service, or cash) controlled by the entity as the result of a past event where the resources will be used by the entity to achieve its goals in the future. Assets can be either financial or non-financial. Assets can be either tangible or intangible. (B) *Recognition*: Assets should be recognized to the extent that they are material, meet the definition of ‘asset’, and the appropriate valuation (see next item) can be measured reliably. (C) *Valuation*: The federal position statement is not a statement of market values. Unless resources are held for re-sale, asset valuation should be based on the amount invested in the resource, adjusted for use to date; i.e., historical cost based. To the extent the historical cost is unknown, some estimate of cost is better than assuming $0. To the extent that assets are maintained for indefinite life, they need not be depreciated. (We should also consider application of the GASB asset impairment guidelines). If resources are held for re-sale, the asset should be valued at estimated net realizable value.

The Board suggested replacing the term “goals” in Mr. Patton’s definition with the phrase “service potential.” Mr. Mosso asked that the notion “that some assets are not used yet they are usable” be incorporated into the definition of an asset. Mr. Patton characterized his definition as a working draft. Further, he acknowledged that the valuation section could be expanded to deal with monetary assets.

Adjournment

The meeting adjourned at PM.

Thursday, April 24, 2003

Agenda Topics

- **Technical Bulletin on Homeland Security Act**

Ms. Comes opened the discussion of responses to the exposure draft by noting that there were no objections to the proposal. Most respondents sought either (1) clarifying changes or (2) responses to additional questions. Ms. Comes explained that providing response to additional questions would require investment of additional staff resources and possibly trigger a need for a new exposure draft. Given the time sensitive nature of the issue and the need to focus on other projects, Ms. Comes recommended that the scope of the technical bulletin be on the broad issue of attaining comparable net cost information.

Ms. Comes presented her proposed actions on the main issues raised by respondents. The issues are listed below with staff recommendation and Board discussion.

Issue 1: With respect to property, plant and equipment (PP&E) transferred, questions were:

> Should a capitalization threshold be applied to the net book value upon transfer?
>
> Should the acquisition date be adjusted to the transfer date?
>
> Should the gross book and associated accumulated depreciation be recorded or should the PP&E be booked at “net”?

Ms. Comes referenced SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 31 and SFFAS 7, *Accounting for Revenue and Other Financing Sources,* paragraph 74. and the glossary definition for “book value.[1]”. She recommended that the technical bulletin not include any language that directs preparers regarding the mechanics of getting to book value. Permitting preparers to select the best means to accomplish the goal of “book value” is appropriate.

Members agreed that no additional guidance would be offered.

Issue 2: Should there be a requirement to segregate custodial revenue related to transferred entities from custodial revenue from continuing operations in legacy agency financial statements?

Ms. Comes noted that there is nothing preventing preparers from making this distinction. However, there is no existing standard requiring it nor do FAS 144 requirements extend to this statement (due to the distinction between “results of operations” and custodial reporting). While the distinction may be useful, Ms. Comes did not believe that it was significant enough to warrant investment of resources in providing additional guidance in light of the associated due process requirements.

Members agreed.

Issue 3: Respondents asked if transfers in or out related to transferred entities should be reported separately from other transfers in or out?

Ms. Comes recommended and the Board did not object to not addressing this suggestion in this technical bulletin.

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[1] BOOK VALUE The net amount at which an asset or liability is carried on the books of account (also referred to as carrying value or amount). It equals the gross or nominal amount of any asset or liability minus any allowance or valuation amount.

Issue 4: How should the "appropriation used" line be segregated? Should the "appropriation used" amount associated with the foregoing "Net Cost of Transferred Operations" amount be reflected on a separate line in the legacy agency's financial statements as "appropriation used to fund Net Cost of Transferred Operations?"

Ms. Comes recommended that this technical bulletin not address assignment of financing sources to the cost of discontinued or continuing operations. The Board did not object.

Issue 5: How should an entity that was formerly not a component of a larger department but that is to become a component of DHS (i.e., the Federal Emergency Management Agency (FEMA)) address reporting its “legacy” operations?

Ms. Comes described this as an operational issue rather than a reporting issue. For example, FEMA’s October 1, 2002 to February 28, 2003 (assumed transfer date) amounts would be consolidated directly to the Consolidated Financial Report of the US Government and its March 1, 2003 to September 30, 2003 results need to be consolidated to the Department of Homeland Security. The operational issues result from the need to submit these amounts and ensure that appropriate audit assurance is attained.

Mr. Calder and GAO staff from the audience noted that this was an audit issue and provided some background information on the current plans for FEMA. After a brief discussion, all members agreed that the issue was not an accounting standards issue.

Issue 6: Should the Board preclude the use of APB 20 as it relates to changes in federal entities? That is, should the Technical Bulletin be extended to all changes in entity?

Ms. Comes recommended and the Board agreed that this proposal should be added to the list of potential future projects.

Ms. Comes indicated that changes would be made to the exposure draft and it would be provided to members for a brief comment period. Following resolution of any Board comments, she would submit it to them for a 15-day period. At the conclusion of the 15-day period, the Technical Bulletin would be issued if a majority of members do not object.

- **Stewardship Land and Heritage Assets**

Ms. Loughan explained that at the last Board meeting, the Heritage Assets and Stewardship Land project was reintroduced. This project evolved as part of the Board’s overall project of reviewing and re-categorizing the stewardship elements to fit the categories identified in the traditional auditing model. At the February meeting, the Board requested additional information on the background of the Board’s decision to review and re-categorize the stewardship elements. Additionally, the Board requested that staff prepare a summary of the remaining Required Supplementary Stewardship Information (RSSI) elements and reporting requirements.

Staff explained that this month's Board binders included a summary prepared by staff explaining factors leading up to the Board's decision to re-categorize elements of RSSI. Staff discussed the key issues surrounding the Board's decision, which included that users may not understand the significance of the information and that existing auditing standards do not address RSSI. In addition, staff included a copy of the *PV on Eliminating the Category "Required Supplementary Stewardship Information"* as it provides additional detail on the issue. Staff explained that the PV was issued in December 2000 and the Board received 20 comment letters, with a majority wishing to retain the RSSI category. However, after considering the comments and holding a public hearing on the matter, the Board continued to believe that avoiding the use of RSSI where it is not essential would eliminate potential confusion and ambiguity.

Mr. Schumacher asked the staff to elaborate on AICPA's involvement with the RSSI re-categorization project. Staff explained that the AICPA had briefed the Board on several occasions regarding audit issues with RSSI and had even formed a task force. However, the task force has not developed any guidance to date. Staff also explained that after consulting with AICPA, it was clear that if the Board's belief was that the information was essential to fair presentation and that the intent would be for an auditor to consider a qualified or adverse opinion when such information was missing or materially misstated, then this would be best assured by designating such information as integral part of the basic financial statements. Other Board members noted that they believe that once the Board designates the information as basic, the audit community will develop guidance.

Mr. Anania stated that it was his understanding that the Board had wanted RSSI information to be subject to some higher level of audit coverage (compared to RSI.) Mr. Calder explained that it would be accurate to say that some of the Board believed that and others believed less audit coverage would be appropriate. Staff explained that looking at certain excerpts from the standards and concepts that there may have been differences of opinion as to what level of audit coverage was appropriate. Mr. Anania explained that again some of these issues that the Board is struggling with does go back to the Board's concepts and objectives.

Staff explained that tab 2 of the Board binder contained a chart prepared by staff detailing the stewardship categories, specific elements and the current disposition of each. The chart enabled the Board to have a snapshot of the progress of re-categorizing RSSI and what remains. Mr. Anania asked if it was the Board's intent to begin a project to reclassify the stewardship investment elements—nonfederal physical property, human capital, and research and development. The Executive Director explained that it was in fact a project that will be addressed after completion of the Heritage Assets and Stewardship Land project. The Chairman confirmed that it was the Board's intent to go forward and reclassify all elements of RSSI. Staff also provided a brief explanation of the remaining items and explained that specific details for each, including a description, reporting requirements and measurement were included in tab 3 of the Board binders.

Staff explained that tab 4 of the binders contained an Analysis of Citations that link Heritage Assets and Stewardship Land to Fair Presentation. Staff discussed that the analyses was prepared by staff and the AAPC Stewardship Workgroup in June 2000 and was included to provide the Board with a complete view of differing support from within the standards and concepts on whether heritage assets and stewardship land is essential for fair presentation. Mr. Patton explained that he believes part of the problem may be the Board's commitment to focus strictly on reclassification versus expanding the scope somewhat to address some of the other issues, such as whether the items are balance sheet items. The Chairman stated that he wanted to reconfirm that it is the Board's intent to strictly look at the re-classification to basic or RSI at this time and that the Board could always come back to look at issues that may need to be addressed further.

Mr. Patton also stated that it was his understanding that it was the Board's intent, along with the Concepts project, to look at the asset definition in conjunction with an existing project. Mr. Patton asked if the Board had decided whether to do this in the natural resources or heritage assets and stewardship land project or defer the effort. The Executive Director explained that it may be appropriate to have discussion of the definition of asset as part of the projects but that it would not be appropriate to stop work on these projects as there appears to be agreement by the Board that these are assets. The Executive Director did note that there may be measurement issues with Heritage Assets and Stewardship Land, but that could be handled within the concepts project. Mr. Schumacher asked if the Board does decide to make the Heritage Assets and Stewardship Land information basic, how would the measurement issue be resolved. The Chairman noted that the same information would continue to be reported. Specifically, there would be a line item on the balance sheet referencing a note disclosure that would contain the non-financial information that is currently being reported as RSSI.

Staff provided an overview of the staff prepared working Exposure Draft *Heritage Assets and Stewardship Land: Reclassification from Required Supplementary Stewardship Information.* Staff explained that the working ED only addresses the reclassification issue and that if the Board does decide to expand the scope of the project to include other issues, the ED can be expanded to include other areas. Staff explained that the ED proposes that heritage assets and stewardship land information be reported as basic information, except for condition reporting , which is currently, and should remain, Required Supplementary Information. Specifically, the ED provides for a line item to be shown on the balance sheet for significant heritage assets and stewardship land, but no financial amount should be shown. Instead, the line item would reference a note disclosure that would provide the current minimum reporting requirements consistent with those in SFFAS No. 8.

Staff supported its proposal to classify the information as basic with the following reasons (as also included in the Basis for Conclusions of the draft ED):

- Heritage assets and stewardship land are considered assets and a defined category of PP&E.

- Information on the assets is crucial to understanding the entirety of an entity's financial condition.
- Accountability for heritage assets and stewardship land requires more audit scrutiny than would be necessary if it were considered RSI.
- This classification would be consistent with existing standards issued by GASB and FASB. There is also existing audit guidance available in this area.
- The reliability and availability of the data has greatly improved because entities have had several years to report on stewardship. Also, the classification of this heritage asset and stewardship land information as basic should not limit the information entities choose to present or prevent the continuation of informative and meaningful displays of information. The Board notes that preparers will continue to have the option of voluntarily presenting supplementary information beyond what is required as other accompanying information.

Staff requested the Board's input and comments on the working draft ED. Mr. Patton stated that he believed the statement that heritage assets and stewardship land are assets does raise the question that "if they are assets, why aren't we recognizing them on the balance sheet instead of in a note disclosure with quantity information?" Mr. Patton stated that although he does agree that they are assets, the current wording does raise questions, especially given the narrow focus of the proposed ED. The Chairman stated that staff needs to expand the discussion in the ED to include the notion that while they are assets and should be on the balance sheet, we currently don't have adequate financial measurement.

Mr. Anania stated that the Board should discuss if they want to have a line display for items considered an asset or a liability by definition, but for which we can't get recognition because of unreliable measurement. Additionally, he explained that the Board should be consistent on both the asset and liability side. He added that it is a very different type of reporting model than used in other sectors. However, Mr. Patton suggested that it is comparable to FASB. Staff also noted that the approach is consistent with the private sector (FAS 116) and GASB's handling of these types of assets and that museums do include a line item on the balance sheet for collections with no dollar item. However, the main difference is that they do encourage capitalization and recognition.

Mr. Reid brought up the fact that in the past, the Board had issued an ED that would make SFFAS No. 8 applicable to the CFR. Specifically, SFFAS No. 8 did not provide an effective date for the reporting requirements at the CFR level. Mr. Reid questioned if perhaps some of the language of the prior ED should be included in this current ED. Staff explained that SFFAS No. 24 *Selected Standards for the Consolidated Financial Report of the United States Government,* makes the assertion that unless a standard states otherwise it is applicable to the CFR. Therefore, the proposed ED would be applicable to the CFR unless there was explicit language stating otherwise. The Board agreed that the proposed ED would take care of ensuring that the requirements are also applicable to the CFR.

Mr. Anania asked if the Board has a preference on the use of ‘material’ versus ‘significant’ in the text of the standards. It was the Board’s preference to use the term ‘significant’ versus ‘material’ and staff agreed to make changes accordingly. Mr. Anania also suggested that staff revise the section of the Executive Summary addressing how the proposal contributes to meeting the federal reporting objectives by removing any reference to audit coverage. Staff agreed to remove that language and only refer to the specific objectives from the concept statements.

Mr. Calder suggested that the Board discuss the issue of presenting a line item on the balance sheet and the way that it is articulated. Specifically, he does not prefer to prescribe line items as the Board may end up with a multi-page balance sheet with prescribed line items for many things. He suggested perhaps one line item for these types of things or for certain categories and it should be described differently in the proposed ED. The Chairman requested staff to draft language that would accomplish this.

The Board agreed with the proposals made during the meeting and requested that staff revise the proposed ED accordingly and then distribute the revised version for comment.

Adjournment

The meeting adjourned at 12:00 PM