Alternative View
Federal Reserve Funds

1. ___ members of the Board agree with the majority that it is the role of preparers and auditors to make the ultimate decision as to whether an entity should be consolidated in the federal government's GPFFR or reported as a disclosure entity. However, in light of the unique characteristics and activities of the government's central bank, i. e., the Federal Reserve System, these members believe the principles set forth in this exposure draft do not provide assurance that the disclosures for the central bank will be adequate for the risks they take on or represent for the United States Government and its taxpayers.

2. The Federal Reserve System is a significant, critical, and pervasive part of the United States Government. It fulfills many of the sovereign functions enumerated in the Constitution, namely, coin money and regulate the value thereof, borrow money on the credit of the United States. It is authorized, by statute, to:

   - conduct the nation's monetary policy by influencing the monetary and credit conditions in the economy;
   - supervise and regulate banking institutions;
   - maintain the stability of the financial system;
   - provide financial services to the U.S. government and others [1]

3. FASAB's Statement of Federal Financial Accounting Concepts 2, *Entity and Display* (SFFAC 2), was issued in 1995 to provide guidance for determining the reporting entity. It explained why the Federal Reserve System could be considered part of the Federal government reporting entity, but it also recognized that "the organization and functions pertaining to monetary policy are traditionally separated from and independent of the other central government organizations and functions in order to achieve more effective monetary policies and economic results."[2] In order to avoid an inference that the Federal Reserve System was not independent of the Federal government, SFFAC 2 explicitly excluded the Federal Reserve System from the financial reporting entity.

4. Significant changes have occurred since 1995. The Federal Reserve System has increasingly been engaging in a wide variety of transactions with various federal agencies, government-sponsored entities, private-sector corporations, and domestic and foreign banks to maintain the stability of the financial system and contain systemic risks arising in the financial markets, many of which have subjected the U.S. government and taxpayers to significant risks. Moreover, it is unclear how the role of

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[1] Board of Governors of the Federal Reserve System *The Federal Reserve System, Purposes & Functions,* 9th ed., 2005
[2] SFFAC 2, paragraph 47.

the Federal Reserve System may change in the future. Hence, the Board has concluded, in this proposed statement, that under the Control with Risk of Loss or Expectation of Benefit principle stated in paragraphs 24-30, the Federal Reserve System should no longer be excluded from the Federal government reporting entity.

5. The exposure draft concludes that the extent of disclosure for each included entity is dependent on whether the entity is consolidated or reported as a disclosure entity. The disclosures required of consolidation entities are guided by Statement of Federal Financial Accounting Concepts No. 6 *Distinguishing Basic Information, Required Supplementary Information and Other Accompanying Information* and the various Statements on Federal Financial Accounting Standards directed to specific accounting, financial reporting and disclosures topics. This guidance was developed over time when the Federal Reserve System was not considered part of the federal reporting entity and thereby does not take into account the Federal Reserve System's unique and expanding characteristics. Were the Federal Reserve System to be consolidated rather than reported as a disclosure entity, as stated in paragraph 62, the extent of disclosures would be determined under existing GAAP. The question the ___ members raise is whether existing GAAP is sufficient to disclose the unique risks the Federal Reserve Systems presents for the United States Government.

6. The disclosures required of disclosure entities are based on six factors and three objectives stated in this proposed statement, which were developed to reflect the circumstances associated with various types of disclosure entities, but not specific to a central bank function. The Stewardship objective for Federal financial reporting states "Federal financial reports should assist users in assessing the impact on the country[3] of the government's operations and investments for the period and how, as a result, the government's and the nation's financial condition has changed and may change in the future" and **w**hether government operations have contributed to the nation's current and future well-being.[4] The ___ members do not believe that these objectives can be met with disclosures that do not encompass the unique role and activities of the central bank.

7. The ___ members believe that to ensure that federal financial statements satisfy the Stewardship and other objectives with respect to the central bank, the following additional disclosures should be incorporated into the exposure draft:

    - the bank's unique organizational and governance structure and how that structure provides the bank with greater independence and insulation from political influence;

    - the bank's significant monetary and fiscal policy activities, such as purchases of Treasury securities, mortgage-backed securities, and the debt of

[3] The "country" and the "nation" are broader than the government. Indeed, the government exists to serve the country and the nation.
[4] SFFAS 1, paragraphs 134 and 143.

government-sponsored entities; central bank liquidity swaps; investments made in consolidated variable investment vehicles, and other lender of last resort activities, with disclosure for each, why and how the activity was undertaken, and trends in the level of activity; and

- the bank's other roles and responsibilities, such as supervising and regulating banking institutions and providing financial services to depository institutions, the government, and foreign official institutions.

QUESTION: Do you agree or disagree that the unique characteristics, financial materiality, significance, and pervasiveness of the central bank merits specific disclosures to reflect the unique risks the central bank function presents to the United States Government and its taxpayers?

Alternative View
Receiverships, Conservatorships, Intervention Entities

1. ___ members believe the proposed standard presents an expanded view of the entity that will result in organizations being included in the reporting entity that do not carry out the sovereign functions of the Federal government. Additionally, they believe that the proposed standard fails to address needed disclosures unique to receiverships, conservatorships, and intervention entities

2. Specifically, Statement of Federal Financial Accounting Concepts (SFFAC) 2, *Entity and Display,* established that for financial reporting purposes, any entity listed in the Budget would be conclusively considered as part of the entity. It then identified "Exercises a sovereign power of the government to carry out federal functions" as the first indicative criteria for whether an organization should be considered part of the reporting entity. In developing this proposed standard, however, the Board chose "In the budget," "Ownership," and "Control with risk of loss or expectation of benefit" as the principles for determining whether an organization should be considered part of the reporting entity. While the Board briefly considered including "Fulfills a sovereign function" as one of the principles, that proposal was rejected.

3. In order to ensure the GPFFR reports all the potential losses and risks that could affect the entity, the Board applied the "ownership" and "control with risk of loss or expectation of benefit" principles to the banks taken into receivership by the Federal Deposit Insurance Corporation (called receiverships); the two organizations, FannieMae and FreddieMac, taken into conservatorship by the Federal Housing Finance Agency (called conservatorships); and several organizations in which, in 2008-2009, the federal government took an equity position, purchased outstanding loans, and/or otherwise injected cash in order to prevent a business failure (called intervention entities). Although the federal government established ownership or control over each of these entities, it did so only to avoid adverse impacts on the nation's economy, commerce, manufacturing base, etc. These actions by the federal government did not make these organizations part of the federal government any more than if the federal government had exercised its regulatory authority over them.

4. An alternative view held by ___ members of the Board is that receiverships, conservatorships, and intervention entities do not carry out sovereign functions and SFFAC 2 did not intend such organizations to be part of the federal government. Moreover, since permanence of the relationship is a fundamental concept when defining parts of an entity, and the government currently deems ownership and control for these organizations as less than permanent, including them as part of the reporting entity simply to ensure the GPFFR reports the risks of loss is a worthy objective, but beyond the scope of this standard.

5. Furthermore, the risk of loss and other exposures associated with the above entities is already required to be disclosed, and has been disclosed for years, by Statement of Federal Financial Accounting Standard 5, *Liabilities,* other Statements of Federal Financial Accounting Standards, and the GAAP hierarchy. On the other hand, neither the existing literature nor the

proposed statement addresses certain additional disclosures associated with receiverships, conservatorships, and intervention entities that some members believe should be required.

6. Finally, the proposed standard for the reporting entity does not address the significant potential risks of loss and exposures associated with all Intervention entities. Some interventions entail the purchase of an equity interest or loans resulting in temporary ownership and/or control. Other interventions, however, particularly those entailing only loan guarantees (e. g., New York City, Chrysler in the late 1970s) do not result in ownership or control and therefore would not be part of the entity under the proposed standard. Moreover, the federal government had a 53% ownership of AIG at the beginning of September, 2012, but sold $xxx,xxx,xxx of common stock in September, 2012 leaving it with a 20% ownership on September 30 2012. Thus, the Federal government no longer had an ownership interest in AIG and would not have been required, under the proposed standard, to report the exposures as of September 30, 2012.

7. Hence, having two Standards—Standard No. 5 dealing with liabilities and other types of risks, and the proposed standard dealing with reporting entities—that address disclosures for receiverships, conservatorships, and intervention entities requires preparers and auditors to apply the criteria from two different standards without achieving any additional disclosures. Pushing this Standards overload onto preparers and auditors is not appropriate, particularly in an era of constrained resources.

8. The alternative view proposes that these problems can be corrected by removing receiverships, conservatorships, and intervention entities from the proposed standard by 1) adding a fourth principle for determining whether an entity should be included in the reporting entity -- namely that it fulfills a sovereign function; and 2) stating that less than permanent receiverships, conservatorships, and intervention entities are not part of the entity.

9. Furthermore, the Board's already-initiated project on risk assumed should be expanded to specifically address the risks of loss emanating from all receiverships, conservatorships, and interventions, and particularly the risks and other disclosures not already provided for in other standards and the GAAP hierarchy. Specifically, it should include not just interventions deemed as temporarily owned or controlled, but also those in which the federal government's intervention is in the form of a loan or loan guarantee, and thus there is no ownership or control. Examples, as stated, are New York City and Chrysler in the late 1970s. Equally important, it should consider the need for other important disclosures. Examples are the extent of contingent liabilities associated with the receiverships, conservatorships, and interventions; costs incurred to date; key transactions; and other matters that would not be appropriate to include in a standard written for all non-disclosure entities.

QUESTION: Do you agree or disagree with the alternative view that the reporting entity should be limited to entities that perform a sovereign function, and thereby not include the receiverships, conservatorships, and intervention entities?