



October 8, 2015

Memorandum

To: Members of the Board

From: Melissa L. Batchelor, Assistant Director

Wendy M. Payne

Through: Wendy M. Payne, Executive Director

Subj: DoD Implementation Guidance Request - **Tab B2**¹

MEETING OBJECTIVES

The objective of this session is to review a draft exposure draft, *Establishing Opening Balances for General Property, Plant and Equipment: Amending Statement of Federal Financial Accounting Standards (SFFAS) 6, SFFAS 10, SFFAS 23, and Rescinding SFFAS 35*.

BRIEFING MATERIAL

The staff analysis is attached along with a question for the Board on page 7. You may electronically access all of the briefing material at <http://www.fasab.gov/board-activities/meeting/briefing-materials/>.

Attachment A- Staff Analysis

Attachment B- Draft Exposure Draft, *Establishing Opening Balances for General Property, Plant and Equipment: Amending Statement of Federal Financial Accounting Standards (SFFAS) 6, SFFAS 10, SFFAS 23, and Rescinding SFFAS 35*

Appendix A- History of Project and Board Decisions

¹ The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations.

BACKGROUND

As you may recall, at the August Board meeting staff provided recommendations regarding baseline estimates of general property, plant, and equipment (GPP&E) and the Board provided feedback. The Board tentatively agreed to the following:

- Allow deemed cost (estimated historical cost, fair value, or replacement cost) for all GPP&E.
- Provide prospective treatment for internal use software and land.
- Acres of land would be disclosed.

It was agreed staff would develop a draft proposal for the Board's consideration at the October meeting.

NEXT STEPS

Staff will consider the Board member comments on the draft exposure draft and work towards a pre-ballot for the December meeting.

MEMBER FEEDBACK

Please contact me as soon as possible to convey your questions or suggestions. Communication before the meeting will help make the meeting more productive. You can contact me by telephone at 202-512-5976 or by e-mail at batchelorm@fasab.gov with a cc to paynew@fasab.gov.

Attachment A- Staff Analysis

As noted, at the August Board meeting it was agreed staff would develop a draft proposal for the Board's consideration on baseline estimates of general property, plant, and equipment (GPP&E).

See **Attachment B- Draft Exposure Draft (ED) Establishing Opening Balances for General Property, Plant and Equipment: Amending Statement of Federal Financial Accounting Standards (SFFAS) 6, SFFAS 10, SFFAS 23, and Rescinding SFFAS 35** that provides the alternative methods - (1) use of deemed cost to establish opening balances of general PP&E and (2) prospective treatment of land and internal use software.

Consistent with the approach used in SFFAS 48, deemed cost is a surrogate for initial amounts and an acceptable valuation method for opening balances for general PP&E. Use of deemed cost is intended to provide a cost-effective approach to the adoption of SFFAS 6, as amended, where historical records and systems do not support such balances. Permitting a reporting entity to apply alternative valuation methods in establishing opening balances for general PP&E would be most appropriate through the implementation guidance.

Consistent with SFFAS 48, the alternative methods are permitted when presenting financial statements, or one or more line items addressed by this Statement, following generally accepted accounting principles (GAAP) promulgated by the Federal Accounting Standards Advisory Board either (1) for the first-time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method. The application of this Statement based on the second condition is available to each reporting entity *only once per line item* addressed in this Statement. Staff would like to point out the difference in wording with this sentence in the Draft ED as opposed to the wording in SFFAS 48, "The application of this Statement based on the second condition is available *once per reporting entity*." Staff suggests this wording change due to the multiple items included within general PP&E and the reporting entity may choose to assert at different times on different categories of general PP&E presented as individual line items.

The implementation guidance for general PP&E currently resides in several Statements. Staff recommends amending SFFAS 6, SFFAS 10, and SFFAS 23, and rescinding SFFAS 35. Based on these proposed amendments and rescission, all implementation guidance for general PP&E, with the exception of certain provisions applicable to internal use software, will be in SFFAS 6. Providing implementation guidance for all general PP&E in SFFAS 6 will provide comprehensive guidance for establishing opening balances for users, versus reviewing multiple Statements that relate to this topic. There is a detailed discussion for each Statement in the basis for conclusion.

Staff notes this is slightly different from the approach that was taken with SFFAS 48 because SFFAS 3 did not have implementation guidance. Therefore, there was no previous implementation guidance that could be amended. Therefore, at the start of that project (SFFAS 48) staff did not envision it as practical to revise implementation guidance as proposed in this project.

Question for the Board:

Does the Board agree with the staff recommended approach—the proposed Statement would amend SFFAS 6, SFFAS 10, and SFFAS 23, and rescind SFFAS 35 by providing implementation guidance to allow a reporting entity to apply alternative valuation methods (deemed cost to establish opening balances of general PP&E and prospective treatment of land and internal use software) in establishing opening balances for general PP&E?

There were a few specific areas that staff would like to ask for Board's feedback as there may be some options to consider:

Land

As you recall, when the Board discussed land in August, the tentative decision was to provide for a prospective treatment for land. Instead, disclosures would reveal the acres of land and changes in those acres over time. This proposal is based on the cost associated with establishing a deemed cost amount for existing land.

Certain members were concerned about the change for a large Department, its consequences on the government-wide statement and whether this issue should be considered more broadly. Meaning, the members suggested exploring options to improve reporting on land at the government-wide level that could be applied consistently across components.

Considering there was agreement that land is somewhat different than general PP&E and the milestones for completing this project are tight, the Board requested staff propose a question on the issue in the ED (see question #2 for Respondents) and provide an explanation of the issue and position in the basis for conclusions, see paragraphs A25. – A28.

Based on the comments received to the question proposed in the ED, staff would recommend the Board then consider whether adding a project on Land to the 3 Year Plan is appropriate.

Questions for the Board:

Does the Board agree with the staff proposed question and language in the Basis for Conclusions regarding Land?

Government Property in the Hands of Contactors

As described in the Draft ED basis for conclusions, government property in the hands of contactors includes government furnished equipment and contractor acquired equipment. DoD has identified this as an issue area and plans to provide a document regarding their challenges and concerns.

Staff anticipates receiving the paper by **October 14, 2015** and will forward this to the Board. In addition, DoD representatives will be available to answer member questions at the Board meeting.

As explained in the basis for conclusions regarding this area, previous Boards believed the accounting treatment for such assets should be consistent with general PP&E since there is no conceptual difference. Further, most would agree there should be accountability over government owned assets in the hands of others. DoD has briefed staff on their concerns regarding the feasibility and cost of obtaining needed information under current contracts.

The language provided in the Draft ED paragraphs A19- A22. provides more detail on this issue. Absent the paper from DoD, staff is unable to provide a complete analysis. However, at this point, staff sees no reason to justify a different treatment than the application of the alternative valuation method or deemed cost that is applicable to general PP&E under the Draft ED.

Question for the Board:

Absent further justification from DoD, does the Board agree that government property in the hands of contactors should be treated consistently as general PP&E? (Therefore, the application of the alternative valuation method (deemed cost) would be applicable in establishing opening balances.)

Note: Staff suggests after receiving the DoD paper that Board members provide any questions they may have for DoD to staff in advance of the meeting.

Internal Use Software (IUS)

At the August meeting, the Board agreed to allow for prospective treatment of IUS. The recommendation was based on several factors, including a specific request submitted by DoD for this treatment for this specific category. Staff's analysis supported such request and described the unique aspects to this category of general PP&E. Staff's analysis in August explained that a similar treatment that was provided when SFFAS 10 was established may be justified. Staff also suggested it would be cost-beneficial for prospective treatment of IUS because it typically has a shorter useful life than other assets and the fact it is a soft asset that is harder to inventory when compared to tangible assets.

Since August, based on discussions with DoD, staff determined that it would be best to provide optimum flexibility within the proposed language. Considering that DoD is a large and complex Department, there might be component reporting entities that currently receive clean audit opinions, charge rates, or may not want to apply the prospective treatment.

Therefore, staff recommends the Statement allow for the following alternatives in establishing opening balances for internal use software:

1. **Deemed cost** or:
2. **Prospective application.** If the reporting entity elects prospective treatment, the reporting entity should choose between the following in establishing the opening balance of IUS under development at the opening balance date:
 - a) Exclude all internal use software, inclusive of that under development at the opening balance date, from the opening balance.
 - b) Exclude IUS in service from the opening balance but include amounts related to IUS under development at the opening balance date. [IUS under development would be recognized in opening balances based on the provisions in SFFAS 10 or on the alternative valuation.]

Because a reporting entity may have multiple component reporting entities selecting different alternatives, a reporting entity may establish an opening balance based on a combination of these alternatives. However, application of a particular alternative must be consistent within each of the component reporting entities prior to consolidation. The disclosures for IUS also contains the following requirement which differs from the general PP&E disclosures "In the event different alternatives are applied by component reporting entities consolidated into a larger reporting entity, the alternative adopted by each significant component should be disclosed."

Question for the Board:

Does the Board agree with staff recommended alternatives and related disclosure in establishing opening balances for internal use software?

Board Member Questions

- 1. Does the Board agree with the staff recommended approach—the proposed Statement would amend SFFAS 6, SFFAS 10, and SFFAS 23, and rescind SFFAS 35 by providing implementation guidance to allow a reporting entity to apply alternative valuation methods (deemed cost to establish opening balances of general PP&E and prospective treatment of land and internal use software) in establishing opening balances for general PP&E?**
- 2. Does the Board agree with the staff proposed question and language in the Basis for Conclusions regarding Land?**
- 3. Absent further justification from DoD, does the Board agree that government property in the hands of contactors should be treated consistently as general PP&E? (Therefore, the application of the alternative valuation method (deemed cost) would be applicable in establishing opening balances.)**
- 4. Does the Board agree with staff recommended alternatives and related disclosure in establishing opening balances for internal use software?**
- 5. Does the Board have any other questions or comments regarding the draft exposure draft, Establishing Opening Balances for General Property, Plant and Equipment: Amending Statement of Federal Financial Accounting Standards (SFFAS) 6, SFFAS 10, SFFAS 23, and Rescinding SFFAS 35?**
- 6. Does the Board want to move to a pre-ballot Draft Exposure Draft?**



Federal Accounting Standards Advisory Board

**ESTABLISHING OPENING BALANCES
FOR GENERAL PROPERTY PLANT
AND EQUIPMENT:**

AMENDING STATEMENT OF FEDERAL FINANCIAL ACCOUNTING
STANDARDS (SFFAS) 6, SFFAS 10, SFFAS 23, AND
RESCINDING SFFAS 35

Statement of Federal Financial Accounting Standards

Exposure Draft

Written comments are requested by [date 90 days after issuance]

Month day, year

Working Draft – Comments Are Not Requested on This Draft

THE FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD

The Secretary of the Treasury, the Director of the Office of Management and Budget (OMB), and the Comptroller General, established the Federal Accounting Standards Advisory Board (FASAB or “the Board”) in October 1990. FASAB is responsible for promulgating accounting standards for the United States Government. These standards are recognized as generally accepted accounting principles (GAAP) for the federal government.

An accounting standard is typically formulated initially as a proposal after considering the financial and budgetary information needs of citizens (including the news media, state and local legislators, analysts from private firms, academe, and elsewhere), Congress, federal executives, federal program managers, and other users of federal financial information. The proposed standards are published in an Exposure Draft for public comment. In some cases, a discussion memorandum, invitation for comment, or preliminary views document may be published before an exposure draft is published on a specific topic. A public hearing is sometimes held to receive oral comments in addition to written comments. The Board considers comments and decides whether to adopt the proposed standard with or without modification. After review by the three officials who sponsor FASAB, the Board publishes adopted standards in a Statement of Federal Financial Accounting Standards. The Board follows a similar process for Statements of Federal Financial Accounting Concepts, which guide the Board in developing accounting standards and formulating the framework for federal accounting and reporting.

Additional background information is available from the FASAB or its website:

- [“Memorandum of Understanding among the Government Accountability Office, the Department of the Treasury, and the Office of Management and Budget, on Federal Government Accounting Standards and a Federal Accounting Standards Advisory Board.”](#)
- [“Mission Statement: Federal Accounting Standards Advisory Board”](#), [exposure drafts](#), [Statements of Federal Financial Accounting Standards and Concepts](#), [FASAB newsletters](#), and other items of interest are posted on FASAB’s website at: www.fasab.gov.

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Federal Accounting Standards Advisory Board

ISSUE DATE

TO: ALL WHO USE, PREPARE, AND AUDIT FEDERAL FINANCIAL INFORMATION

Your comments on the exposure draft of a proposed Statement of Federal Financial Accounting Standards, entitled *Establishing Opening Balances for General Property, Plant and Equipment: Amending Statement of Federal Financial Accounting Standards (SFFAS) 6, SFFAS 10, SFFAS 23, and Rescinding SFFAS 35*, are requested. Specific questions for your consideration appear on page 7 but you are welcome to comment on any aspect of this proposal. If you do not agree with the proposed approach, your response would be more helpful to the Board if you explain the reasons for your position and any alternative you propose. Responses are requested by DUE DATE.

All comments received by the FASAB are considered public information. Those comments may be posted to the FASAB's website and will be included in the project's public record.

Mail delivery is delayed by screening procedures. Therefore, please provide your comments in electronic form by e-mail to fasab@fasab.gov. If you are unable to e-mail your responses, we encourage you to fax the comments to (202) 512-7366. Alternatively, you may mail your comments to:

Wendy M. Payne, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6H19
441 G Street, NW, Suite 6814
Washington, DC 20548

We will confirm receipt of your comments. If you do not receive confirmation, please contact our office at 202.512.7350 to determine if your comments were received.

The Board's rules of procedure provide that it may hold one or more public hearings on any exposure draft. No hearing has yet been scheduled for this exposure draft. **or** A public hearing has been scheduled at 9:00 AM on Month Day, Year, in Room 7C13 at the GAO Building, 441 G Street, NW, Washington, D.C.

Notice of the date and location of any public hearing on this document will be published in the Federal Register and in the FASAB's newsletter.

Sincerely,

Tom L. Allen
Chairman

EXECUTIVE SUMMARY

WHAT IS THE BOARD PROPOSING?

This Statement provides implementation guidance to allow a reporting entity to apply alternative methods in establishing opening balances for general property, plant and equipment (PP&E). To do so, it amends Statement of Federal Financial Accounting Standards (SFFAS) 6, *Accounting for Property, Plant and Equipment*; SFFAS 10, *Accounting for Internal Use Software*; and SFFAS 23, *Eliminating the Category National Defense Property, Plant and Equipment*; and rescinds SFFAS 35, *Estimating the Historical Cost of General Property, Plant and Equipment: Amending Statements of Federal Accounting Standards 6 and 23*. The alternative methods include (1) use of deemed cost to establish opening balances of general PP&E and (2) prospective treatment of land and internal use software.

The alternative methods are permitted when presenting financial statements, or one or more line items addressed by this Statement, following generally accepted accounting principles (GAAP) promulgated by the Federal Accounting Standards Advisory Board either (1) for the first-time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method. The application of this Statement based on the second condition is available to each reporting entity only once per line item addressed in this Statement.

HOW WOULD THIS PROPOSAL IMPROVE FEDERAL FINANCIAL REPORTING AND CONTRIBUTE TO MEETING THE FEDERAL FINANCIAL REPORTING OBJECTIVES?

This Statement is intended to provide alternative methods when historical records and systems do not provide a basis for valuation of opening balances in accordance with SFFAS 6, 10, 23, and 35. The alternatives are intended to reduce the barriers to and cost of adopting GAAP.

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QUESTIONS FOR RESPONDENTS

The Board encourages you to become familiar with all proposals in the Statement before responding to the questions in this section. In addition to the questions below, the Board also would welcome your comments on other aspects of the proposed Statement. Because the proposals may be modified before a final Statement is issued, it is important that you comment on proposals that you favor as well as any that you do not favor. Comments that include the reasons for your views will be especially appreciated.

The Board believes that this proposal would improve federal financial reporting and contribute to meeting the Federal financial reporting objectives. The Board has considered the perceived costs associated with this proposal. In responding, please consider the expected benefits and perceived costs and communicate any concerns that you may have in regard to implementing this proposal.

The questions in this section are available in a Word file for your use at www.fasab.gov/exposure.html. Your responses should be sent by e-mail to fasab@fasab.gov. If you are unable to respond by e-mail, please fax your responses to (202) 512-7366. Alternatively, you may mail your responses to:

Wendy M. Payne, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6H19
441 G Street, NW, Suite 6814
Washington, DC 20548

All responses are requested by [insert date].

- Q1. The Board proposes a reporting entity be permitted to apply an alternative valuation method in establishing opening balances for general property, plant and equipment when presenting financial statements or one or more line items addressed by this Statement following generally accepted accounting principles (GAAP) promulgated by the Federal Accounting Standards Advisory Board (FASAB) either (1) for the first-time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method.

The proposed Statement describes the alternative valuation method and related disclosures.

a) Do you agree or disagree with the proposal to permit opening balances of general PP&E to be valued based on deemed cost? Please provide your rationale.

b) Do you agree or disagree that the related disclosures are appropriate? Please provide your rationale.

- Q2. The Board proposes to amend Statement of Federal Financial Accounting Standards (SFFAS) 6, *Accounting for Property, Plant and Equipment*, so that land categorized as general PP&E may be excluded from the opening balances of general PP&E. Instead, disclosures would reveal the acres of land and changes in those acres over time. This proposal is based on the cost associated with establishing a deemed cost amount for existing land.

Some members suggested valuing existing land holdings based on a set amount per acre of land. For example, one study estimated the land value in the United States at roughly \$4.5 trillion in the third quarter of 2009. Since the number of acres in the United States is almost 2.3 billion, this equates to approximately \$2,000 per acre. (Land values vary greatly based on location, potential use, and availability and cost of financing.) These members are interested in receiving comments on the usefulness of a general valuation approach that could be applied government-wide. (See paragraphs A27 and A28 in the Basis for Conclusions.)

- a) **Do you agree or disagree with the proposal to exclude land from the opening balances of general PP&E? Please provide your rationale.**
- b) **Do you agree or disagree that the related disclosures are appropriate? Please provide your rationale.**
- c) **Do you believe the Board should consider cost-effective options for valuing land on a government-wide basis? Please provide your rationale and any suggestions you have for improving current reporting on land.**

- Q3. The Board proposes to amend SFFAS 10, *Accounting for Internal Use Software*, to allow a reporting entity to choose among alternatives in establishing an opening balance for internal use software when presenting financial statements or one or more line items addressed by this Statement following generally accepted accounting principles (GAAP) promulgated by the Federal Accounting Standards Advisory Board (FASAB) either (1) for the first-time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method. The Statement provides for selecting between (1) an alternative valuation method of deemed cost that is consistent with that provided for all general PP&E and (2) prospective application.

The proposed Statement describes the alternatives and related disclosures. (See Statement paragraphs 11-12 and A29-A33, and A42-A45 in the Basis for Conclusions.)

- a) **Do you agree or disagree with the proposal to allow a reporting entity to choose among alternatives in establishing an opening balance for internal use software? Please provide your rationale.**
- b) **Do you agree or disagree that the related disclosures are appropriate? Please provide your rationale.**

Q4. The Board proposes to rescind SFFAS 35, *Estimating the Historical Cost of General Property, Plant and Equipment: Amending Statements of Federal Accounting Standards 6 and 23*, because this Statement would provide comprehensive guidance for establishing opening balances. The Board has incorporated the relevant components of SFFAS 35 in the proposed guidance in this Statement. (See Statement paragraph 16 and A37- A41 in the Basis for Conclusions.)

**a) Do you agree or disagree with the proposal to rescind SFFAS 35?
Please provide your rationale.**

INTRODUCTION

PURPOSE

1. This Statement amends Statement of Federal Financial Accounting Standards (SFFAS) 6 *Accounting for Property, Plant and Equipment*, SFFAS 10, *Accounting for Internal Use Software* and SFFAS 23, *Eliminating the Category National Defense Property, Plant and Equipment*, and rescinds SFFAS 35, *Estimating the Historical Cost of General Property, Plant and Equipment: Amending Statements of Federal Accounting Standards 6 and 23* by providing implementation guidance to allow a reporting entity to apply alternative methods in establishing opening balances for general property, plant and equipment (PP&E). General PP&E is any property, plant, and equipment used in providing goods or services.¹
2. The alternative methods permitted by this Statement may be applied when a reporting entity is presenting financial statements or one or more line items addressed by this Statement following generally accepted accounting principles (GAAP) promulgated by the Federal Accounting Standards Advisory Board (FASAB) either (1) for the first-time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method. The application of this Statement based on the second condition is available to each reporting entity only once per line item addressed in this Statement.
3. This Statement provides implementation guidance to allow a reporting entity to apply an alternative valuation method in establishing opening balances for general PP&E in the first reporting period in which the reporting entity makes an unreserved assertion that its financial statements, or one or more line items are presented fairly in accordance with GAAP. Through the amendments it also provides for the prospective treatment of internal use software and land in the first reporting period in which the reporting entity makes an unreserved assertion that its financial statements, or one or more line items, are presented fairly in accordance with GAAP.
4. As a result of these amendments and rescission, all implementation guidance for general PP&E, with the exception of certain provisions applicable to internal use software, will be in SFFAS 6. The Board believes providing implementation guidance for general PP&E other than internal use software in SFFAS 6 will provide a comprehensive guide for users in a single Statement.

MATERIALITY

5. The provisions of this Statement need not be applied to immaterial items. The determination of whether an item is material depends on the degree to which omitting or misstating information about the item makes it probable that the judgment of a reasonable person

¹ For a complete discussion of the definition, characteristics, recognition and measurement principles for general PP&E, see SFFAS 6 paragraphs 21-39. The definition, recognition and measurement principles for internal use software are at SFFAS 10 paragraphs 9-34.

relying on the information would have been changed or influenced by the omission or the misstatement.

PROPOSED STANDARDS

SCOPE

6. This Statement applies when a reporting entity is presenting financial statements or one or more line items addressed by this Statement following generally accepted accounting principles (GAAP) promulgated by the Federal Accounting Standards Advisory Board (FASAB) either (1) for the first-time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method. The application of this Statement based on the second condition is available to each reporting entity only once per line item addressed in this Statement.
7. This Statement may be applied in establishing opening balances² for the reporting period that the reporting entity, taken as a whole, makes an unreserved assertion³ that its financial statements, or one or more line items addressed by this Statement, are presented fairly in accordance with GAAP.
8. Reporting entities that meet either condition in paragraph 4 and elect to apply the alternative valuation method in establishing opening balances permitted by this Statement are subject to the reporting requirements under paragraph 13 of Statement of Federal Financial Accounting Standards (SFFAS) 21: *Reporting Corrections of Errors and Changes in Accounting Principles*.

AMENDMENTS TO SFFAS 6, *ACCOUNTING FOR PROPERTY, PLANT AND EQUIPMENT*

9. This section amends the Implementation Guidance provided in SFFAS 6, *Accounting for Property, Plant and Equipment* as described in the following paragraphs.
10. Paragraph 40 is replaced with:

40. Alternatives Available for Opening Balances.⁴ The following guidance is applicable for the reporting period when the reporting entity is presenting financial statements, or one or more line items addressed by this Statement, following generally accepted accounting

² Opening balances are account balances that exist at the beginning of the reporting period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period. Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments. (See Statement of Federal Financial Accounting Standards (SFFAS) 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials*.)

³ An unreserved assertion is an unconditional statement. (See SFFAS 48.)

⁴ Opening balances are account balances that exist at the beginning of the reporting period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period. Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.

principles (GAAP) promulgated by the FASAB either (1) for the first-time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method. The following should be considered in applying the alternatives for establishing the opening balance:

- i) The alternatives for establishing opening balances may only be applied for the reporting period that the reporting entity, taken as a whole, makes an unreserved assertion⁵ that its financial statements, or one or more line items addressed by this Statement, are presented fairly in accordance with GAAP.
- ii) The application of these alternatives based on the second condition specified in paragraph 40 is available only once per line item to each reporting entity.
- iii) Reporting entities that meet either condition in paragraph 40 and elect to apply any of the alternatives available in establishing opening balances are subject to the reporting requirements under paragraph 13 of Statement of Federal Financial Accounting Standards 21: *Reporting Corrections of Errors and Changes in Accounting Principles*.
- iv) Land. The reporting entity may exclude land from the opening balance of general PP&E.
- v) Alternative Valuation Method. Deemed cost:⁶ is an acceptable valuation method for opening balances of general PP&E. Because the reporting entity may have multiple component reporting entities using various valuation methods simultaneously, deemed cost should be based on one, or a combination, of the following valuation methods:⁷
 - (1) Replacement cost⁸
 - (2) Estimated historical cost (initial amount)--Reasonable estimates may be based on:
 - i. cost of similar assets at the time of acquisition,
 - ii. current cost of similar assets discounted for inflation since the time of acquisition (that is, deflating current costs to costs at the time of acquisition by general price index), or
 - iii. other reasonable methods, including latest acquisition cost and estimation methods based on information such as, but not limited to, budget, appropriations, engineering documents, contracts, or other reports reflecting amounts to be expended.
 - (3) Fair value⁹

⁵ An unreserved assertion is an unconditional statement.

⁶ Deemed cost is an amount used as a surrogate for initial amounts that otherwise would be required to establish opening balances.

⁷ The methods are not listed in order of preference.

⁸ Replacement cost is the amount required for an entity to replace the remaining service potential of an existing asset in a current transaction at the reporting date, including the amount that the entity would receive from disposing of the asset at the end of its useful life. (SFFAC 7, par. 46)

⁹ Fair value is the amount at which an asset or liability could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. (SFFAC 7, par. 38)

- vi) Establishing in-service dates. In some cases, the in-service date must be estimated. In estimating the year that the base unit was placed in service, if only a range of years can be identified then the mid-point of the range is an acceptable estimate of the in-service date.
- vii) Disclosure requirements:
 - (1) A reporting entity electing to exclude land from its general PP&E opening balances must disclose this fact, the number of acres of land held at the beginning of each reporting period, the number of acres added during the period, the number of acres disposed of during the period, the number of acres held at the end of each reporting period, and the number of acres for which an amount is included in general PP&E.¹⁰
 - (2) A reporting entity electing to apply deemed cost in establishing opening balances for general PP&E should disclose this fact and describe the method used in the first reporting period in which the reporting entity makes an unreserved assertion that its financial statements, or one or more line items are presented fairly in accordance with GAAP. Financial statements, or as applicable, reports on line items, of subsequent periods need not repeat this disclosure unless the statements for which deemed cost was applied in establishing opening balances are presented for comparative purposes. No disclosure of the distinction or breakout of amount of deemed cost of general PP&E included in the opening balance is required.

AMENDMENTS TO SFFAS 10, *ACCOUNTING FOR INTERNAL USE SOFTWARE*

11. This section amends the Implementation Guidance provided in SFFAS 10, *Accounting for Internal Use Software*, as described in the following paragraphs.

12. Paragraph 36 is replaced with:

36. Alternatives for Establishing Opening Balances.¹¹ The following guidance is applicable for the reporting period when the reporting entity is presenting financial statements, or the item addressed by this Statement, following generally accepted accounting principles (GAAP) promulgated by the FASAB either (1) for the first-time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative valuation method. The following should be considered in applying an alternative:

¹⁰ The amount will relate to acquisition of land subsequent to the date of the opening balance.

¹¹ Opening balances are account balances that exist at the beginning of the reporting period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period. Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.

- a. Alternatives for establishing opening balances may only be applied for the reporting period that the reporting entity, taken as a whole, makes an unreserved assertion¹² that its financial statements, or the line item addressed by this Statement, are presented fairly in accordance with GAAP and for periods during which it is necessary to correct errors in this opening balance that are discovered in later reporting periods.
- b. The application of this method based on the second condition specified in paragraph 36. is available only once to each reporting entity. Application of the recognition, measurement, and disclosure requirements of this Statement is required during the reporting period when the reporting entity makes an unreserved assertion.
- c. Reporting entities that meet either condition in paragraph 36 and elect to apply any of the alternatives available in establishing opening balances are subject to the reporting requirements under paragraph 13 of Statement of Federal Financial Accounting Standards 21: *Reporting Corrections of Errors and Changes in Accounting Principles*.
- d. Alternatives. A reporting entity may choose among the following alternatives for establishing an opening balance for internal use software. Because a reporting entity may have multiple component reporting entities selecting different alternatives, a reporting entity may establish an opening balance based on a combination of these alternatives. However, application of a particular alternative must be consistent within each of the component reporting entities prior to consolidation.
 - i. Prospective application. The reporting entity may choose prospective application of SFFAS 10. If the reporting entity elects prospective treatment, the reporting entity should choose between the following acceptable alternatives, in establishing the opening balance of IUS under development at the opening balance date:
 - (a) Exclude all internal use software, inclusive of that under development at the opening balance date, from the opening balance.
 - (b) Exclude IUS in service from the opening balance but include amounts related to IUS under development at the opening balance date. IUS under development should be recognized in opening balances based on the provisions of paragraphs 15 thru 27 or on the alternative valuation method provided in paragraph 36.d.ii.
 - ii. Alternative Valuation Method. Deemed cost¹³ is an acceptable valuation method for opening balances of internal use software. See SSFAS 6 paragraph 40 for Implementation Guidance regarding deemed cost.
- e. Disclosure requirements: A reporting entity electing to apply the alternative methods should disclose this fact and describe the alternatives used in the first reporting period in which the reporting entity makes an unreserved assertion that its financial

¹² An unreserved assertion is an unconditional statement.

¹³ Deemed cost is an amount used as a surrogate for initial amounts that otherwise would be required to establish opening balances.

statements, or one or more line items are presented fairly in accordance with GAAP. In the event different alternatives are applied by component reporting entities consolidated into a larger reporting entity, the alternative adopted by each significant component should be disclosed. Financial statements, or as applicable, reports on line items, of subsequent periods need not repeat this disclosure unless the statements for which the alternative for establishing opening balances was applied are presented for comparative purposes. No disclosure of the distinction or breakout of amount of deemed cost of internal use software included in the opening balance is required.

AMENDMENTS TO SFFAS 23, *ELIMINATING THE CATEGORY NATIONAL DEFENSE PROPERTY, PLANT AND EQUIPMENT*

13. This section amends the Implementation Guidance provided in SFFAS 23, *Eliminating the Category National Defense Property, Plant and Equipment*, as described in the following paragraphs.
14. Paragraph 10 is replaced with:
 10. See SFFAS 6 for Implementation Guidance that applies to all general PP&E.
15. Paragraphs 11- 18 of SFFAS 23 are rescinded. (For implementation guidance, see SFFAS 6, as amended.)

RESCISSION OF SFFAS 35, *ESTIMATING THE HISTORICAL COST OF GENERAL PROPERTY, PLANT AND EQUIPMENT: AMENDING STATEMENTS OF FEDERAL ACCOUNTING STANDARDS 6 AND 23*

16. This paragraph rescinds SFFAS 35, *Estimating the Historical Cost of General Property, Plant and Equipment: Amending Statements of Federal Accounting Standards 6 and 23* in its entirety. Provisions from SFFAS 35 were incorporated into the Implementation Guidance of SFFAS 6 as needed.

EFFECTIVE DATE

17. This Statement is effective for periods beginning after September 30, 2016. Earlier implementation is encouraged.

The provisions of this Statement need not be applied to immaterial items.

APPENDIX A: BASIS FOR CONCLUSIONS

This appendix discusses some 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.

PROJECT HISTORY

Department of Defense Implementation Guidance Request Project

- A1. In February 2014, the Department of Defense (DoD) identified several areas of concern for the Federal Accounting Standards Advisory Board (FASAB)'s consideration. The Board agreed to undertake a project to address these areas by providing practical guidance within the framework of existing accounting standards and, where necessary, provide the appropriate guidance to address issues not addressed within the framework of existing accounting standards.
- A2. This Statement is related to the request from DoD for guidance on establishing opening balances for general property, plant and equipment (PP&E). Accounting for the federal government's general PP&E is complex and continues to be a challenge for large federal departments. This topic has been addressed in numerous Federal Accounting Standards Advisory Board (FASAB) Statements and Interpretations as well as guidance issued by the Accounting and Auditing Policy Committee. Statement of Federal Financial Accounting Standards (SFFAS) 6, *Accounting for Property, Plant and Equipment*, SFFAS 10, *Accounting for Internal Use Software*, SFFAS 23, *Eliminating the Category National Defense Property, Plant and Equipment*, and SFFAS 35, *Estimating the Historical Cost of General Property, Plant and Equipment: Amending Statements of Federal Accounting Standards 6 and 23* address the accounting and reporting requirements for general PP&E.
- A3. During the project, Board staff met with officials from DoD, as well as the audit community, to develop an understanding of the issues currently faced by DoD in establishing their baseline for general PP&E. This included discussing valuation methodologies currently employed, difficulties relevant to management assertions and the completion of audit, and the status of implementation of a generally accepted accounting principles (GAAP) compliant system for DoD component.
- A4. Based on the meetings and information provided it was determined that:
- a. DoD financial systems and many aspects of DoD accounting policy for general PP&E has not been in accordance with FASAB GAAP.
 - b. Many organizations and systems are involved in acquiring general PP&E assets.
 - c. DoD has not had consistent procedures related to general PP&E acquisitions or documented processes for retaining source documentation.
 - d. All systems that the DoD has utilized for acquisitions of general PP&E have either never been audited, or when audited had significant deficiencies or material weaknesses related to them.

- e. Capital improvement projects have not been reliably tracked in systems so it is difficult to determine the date they were placed in service, or establish a valuation baseline.
- f. DoD has approximately 440,000 separate real property assets and many real property assets facility built dates are beyond 40 years.
- g. DoD records related to land values are not in a structured, searchable manner. The records are not digitized and accessing them involves searching boxed records in a warehouse. Also, records such as deeds may not be complete and court records often have gaps given the length of time involved.
- h. DoD does not have a complete inventory of its internal use software (IUS) and costs of IUS have not traditionally been captured.
- i. General equipment is a broad category that includes military type equipment and consists of hundreds of thousands of assets.

A5. After considering the status of DoD's efforts and the fact DoD has had numerous years to implement the standards and has shown little progress, the Board discussed the merits of the project. Specifically, one member had concern regarding what the Board's role was and that the Board may be undermining its own credibility by acting to offer relief to DoD because it has been unable to adopt GAAP requirements. The Board acknowledges that appearance is a concern. However, FASAB has been tasked with establishing standards for which the benefits exceed the cost.

A6. The Board noted that while DoD has had numerous years to meet the standards and become GAAP compliant, they have not. Conditions remain that existed when many of these standards were issued and the cost to implement all the standards concurrently is greater than would have been incurred if standards were implemented timely. The goal of this Statement is to avoid expending taxpayer dollars on recreating information that is long past its primary usefulness, which is evaluating major acquisition/construction programs as they are executed and avoiding overstatement of period expense by charging off the cost of acquiring assets as expenses.

A7. The Board believes assisting DoD with establishing a baseline would benefit all parties. Providing a starting point may enable DoD to focus on needed improvements to systems and controls. Establishing a sound financial management system is of primary importance.

A8. The Board also acknowledged that other standard setters have provided guidance for organizations implementing an entire body of standards for a first time. The challenge of establishing opening balances for large public sector entities warrants the flexibilities proposed in this Statement.

ALTERNATIVE VALUATION METHOD AND IMPLEMENTATION GUIDANCE

A9. During deliberation on the project, the Board considered the recently approved SFFAS 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials*. SFFAS 48 permits a reporting entity to apply an alternative valuation method in establishing opening balances for inventory, operating materials and supplies, and stockpile materials. Deemed cost, or the amount used as a surrogate for initial amounts that otherwise would be required to establish opening balances, was the alternative valuation method for valuation of

opening balances in accordance with SFFAS 3, *Accounting for Inventory and Related Property* in SFFAS 48.

- A10. The Board based part of its decision to select deemed cost in SFFAS 48 on International Public Sector Accounting Standards (IPSAS) No. 33, *First Time Adoption of Accrual Basis International Public Sector Accounting Standards*. The International Public Sector Accounting Standards Board (IPSASB) reached several relevant conclusions with IPSAS No. 33:
- a. Use of deemed cost facilitates the introduction of IPSASs in a cost effective way.
 - b. Multiple options for deemed cost are appropriate.
 - c. The use of deemed cost should be restricted to those circumstances where reliable information about the historical cost of the asset is not available.
 - d. Use of deemed cost does not affect fair presentation.
- A11. Consistent with the decisions in SFFAS 48, the Board believes an approach similar is appropriate in this project. Deemed cost is a surrogate for initial amounts and an acceptable valuation method for opening balances for general PP&E. Use of deemed cost is intended to provide a cost-effective approach to the adoption of SFFAS 6, as amended where historical records and systems do not support such balances.
- A12. The Board determined permitting a reporting entity to apply alternative valuation methods in establishing opening balances for general PP&E would be most appropriate through the implementation guidance. The implementation guidance for general PP&E currently resides in several Statements. Accordingly, this Statement amends SFFAS 6, SFFAS 10, and SFFAS 23, and rescinds SFFAS 35 by providing implementation guidance to allow a reporting entity to apply an alternative valuation method in establishing opening balances for general PP&E. Further, based on these amendments and rescission, all implementation guidance for general PP&E, with the exception of certain provisions applicable to internal use software, will be in SFFAS 6. The Board believes providing implementation guidance for all general PP&E in SFFAS 6 will provide a more inclusive approach and comprehensive guide for users versus reviewing multiple Statements that relate to this topic.

AMENDMENTS TO STATEMENT OF FEDERAL FINANCIAL ACCOUNTING STANDARDS

Amendments to SFFAS 6, Accounting for Property, Plant and Equipment

- A13. SFFAS 6 provides the accounting standards for general PP&E and implementation guidance. The implementation guidance for general PP&E currently resides in several Statements due to subsequent amendments to SFFAS 6. To provide implementation guidance allowing a reporting entity to apply alternative methods in establishing opening balances for general PP&E, this Statement amends existing standards to provide all implementation guidance for general PP&E, with the exception of certain provisions applicable to internal use software, in SFFAS 6.

- A14. Having all the general PP&E implementation guidance within SFFAS 6 will provide a more complete guide for users when referencing the Statements versus considering several Statements that have amendments.
- A15. This Statement would amend SFFAS 6 implementation guidance to include alternatives for establishing opening balances. A reporting entity may use deemed cost as an alternative valuation method in establishing opening account balances for general PP&E in SFFAS 6 for the reporting period that the reporting entity first makes an unreserved assertion that its financial statements, or one or more line items addressed by this Statement, are presented fairly in accordance with GAAP.
- A16. This guidance is intended to provide a cost-effective approach to the adoption of SFFAS 6 where historical records and systems do not support such balances. Accordingly, this Statement provides flexibility by permitting use of several measurement attributes and estimates. Deemed costs should be based on one, or a combination, of the following valuation methods: replacement cost, estimated historical cost, reasonable estimates, or fair value. The Board believes this is the most cost effective option.
- A17. Using the DoD example, providing implementation guidance requires consideration of cost-benefit as well as the current resource constraints. For example, DoD has a dual challenge of establishing the baseline and still getting a system capable of capturing the information to capitalize the new general PP&E and therefore updating the information.
- A18. DoD currently uses plant replacement value (PRV) which is based on cost factors such as averages of contractual cost data from the prior three years, commercially available cost data, and models using general price information. While PRV (a replacement cost model) has not been used for financial reporting purposes, DoD officials have stated that this is a model used for decision making and management purposes. This Statement would allow for PRV to be used in establishing the opening balance for real property in current year dollars and not be deflated to the in-service year. PRV is inclusive of capital improvements. Accumulated depreciation would be recognized based on the remaining useful life compared to the original useful life. This would not systematically understate the historical cost since capital improvements would not be deflated. However, by allowing current year costs, it may overstate the historical cost and subsequent years' depreciation expense.
- A19. A challenging issue for reporting entities in establishing opening balances for general PP&E can be government property in the hands of contractors. This may include government furnished equipment and contractor acquired equipment. Previous Boards believed the accounting treatment for such assets should be consistent with that of other assets since there is no conceptual difference. Further, most would agree there should be accountability over government owned assets in the hands of others.
- A20. SFFAS 6 paragraph 18 provides that PP&E includes "property owned by the reporting entity in the hands of others (e.g., state and local governments, colleges and universities, or Federal contractors)" and paragraph 34 (along with footnote 34) elaborates that PP&E shall be recognized when title passes or is delivered to the acquiring entity or to an agent of the entity. For PP&E acquired by a contractor on behalf of the entity (e.g., the entity will ultimately hold title to the PP&E), PP&E shall also be recognized upon delivery or constructive delivery whether to the contractor for use in performing contract services or to the entity.

- A21. During the due process deliberation of SFFAS 23, the issue also came up and a respondent unaware of existing standards encouraged the Board to develop standards that address this type of property because the respondent believed, “accounting control over this property is deplorable.” As discussed in the basis for conclusions to SFFAS 23, the previous Board found that “It is clear that, despite the existence of standards for contractor held assets since late 1995, little progress has been made in resolving the issue. The Board does not believe that deferral of standards related to vast amounts of PP&E will facilitate resolution of the contractual and administrative details needed to reasonably comply with generally accepted accounting principles.”
- A22. The Board understands that certain reporting entities may have long-standing contracts lacking contractual terms and systems needed to accumulate the necessary information. The alternative valuation method—deemed cost—is applicable to general PP&E in the hands of others. Other alternatives to mitigate the cost of properly reporting on such PP&E were considered and the Board concluded **[placeholder – staff anticipates receiving a proposal from DoD regarding this matter on October 14th and will update this section based on Board deliberation]**.
- A23. The Board recognizes that large and complex reporting entities such as DoD may have used a variety of valuation methods prior to the adoption of a GAAP compliant method. Therefore, this Statement allows for deemed cost to include several valuation methods because the reporting entity may have components (1) using different methods simultaneously and/or (2) adopting a method permitted under SFFAS 6 at different times prior to establishing opening balances. Deemed cost may be one of or a combination of valuation methods. However, this Statement requires that the accounting for all activity after the opening balance is established comply with SFFAS 6.
- A24. The purpose of this Statement is to provide an alternative valuation method for this specific situation. Absent a reliable record of transactions related to hundreds of thousands of records and related assets, this is the most cost-effective approach for opening balances while reporting entities such as DoD finalize a sound GAAP compliant financial management system. All activity after the opening balances for general PP&E are established must comply with the recognition, measurement, presentation, and disclosure requirements in SFFAS 6.
- A25. When deliberating general PP&E, the Board considered land somewhat differently from general PP&E. Allocation of the cost of general PP&E, excluding land, among accounting periods is essential to assessing operating performance. Statement of Federal Financial Accounting Concepts (SFFAC) 1, *Objectives of Federal Financial Reporting*, focuses on relating cost to accomplishments in reporting an entity’s operating performance and cost information is of fundamental importance both to program managers in operating their activities efficiently and effectively and to executive and congressional decision makers in deciding on resource allocation. General PP&E will be capitalized and depreciated to provide this information. Because land is not depreciated, the benefits of capitalizing it are primarily in the period of acquisition. That is, the cost of the land is identified so the acquisition can be evaluated and capitalized so the period operating costs are not overstated. In future periods, the ongoing benefit is that accountability for the asset is established.

A26. The Board considered those aspects to the land category and determined the most cost-beneficial approach to establishing an opening balance for land was to permit the reporting entity to exclude land from the opening balance of general PP&E. Meaning this allows for prospective treatment by excluding existing land from its general PP&E opening balance. However, the Board can establish accountability through disclosures. The Board proposed that the reporting entity disclose the adoption of prospective reporting, the number of acres of land held at the beginning of each reporting period, the number of acres added during the period, the number of acres disposed of during the period, the number of acres held at the end of each reporting period, and the number of acres for which an amount is included in general PP&E (the amount will relate to acquisition of land subsequent to the date of the opening balance).

A27. Some members who supported the prospective treatment of land suggested exploring options to improve reporting on land. Current standards provide that only land acquired in connection with development or construction of an item of general PP&E should be treated as general PP&E. As a result, vast amounts of land are not recognized on the balance sheet. Instead, they are disclosed in a note to the balance sheet.

A28. These members would like to explore valuing existing land holdings based on a set amount per acre of land. For example, one study¹⁴ estimated the land value in the United States at roughly \$4.5 trillion in the third quarter of 2009. Since the number of acres in the United States is almost 2.3 billion, this equates to approximately \$2,000 per acre. Challenges in applying this method are many. Land values vary greatly based on location, potential use, and availability and cost of financing. In addition to establishing a relevant initial valuation, members would need to consider whether the valuation should be updated and, if so, how often. Nonetheless, these members are interested in receiving comments on the usefulness of a general valuation approach that could be applied government-wide to both land classified as general PP&E and stewardship land.

Amendments to SFFAS 10, Accounting for Internal Use Software

A29. SFFAS 10 provides accounting standards for internal use software (IUS) used by federal entities. Previously, IUS had been addressed in SFFAS 6, but certain questions remained regarding the issue and the Board decided to review the issue and develop a separate Statement.

A30. IUS addressed by SFFAS 10 includes purchased commercial “off-the-shelf” software, contractor-developed software, and internally-developed software. Under the provisions of SFFAS 10, IUS is classified as general PP&E as defined in SFFAS 6. With the issuance of SFFAS 10, the section on IUS in SFFAS 6 was rescinded and the definition and capitalizable costs for IUS were broadened. SFFAS 10 provided guidance regarding the types of cost elements to capitalize, the timing and thresholds of capitalization, amortization periods, accounting for impairment, and other guidance.

A31. When SFFAS 10 was issued, the previous Board in effect provided for prospective implementation of SFFAS 10 in paragraph 36 by stating that “Cost incurred prior to the initial

¹⁴ Joseph B. Nichols, Stephen D. Oliner, and Michael R. Mulhall. Commercial and Residential Land Prices Across the United States. *Finance and Economics Discussion Series*. Federal Reserve Board. Divisions of Research & Statistics and Monetary Affairs. 2010-16.

application of this statement, whether capitalized or not, should not be adjusted to the amounts that would have been capitalized, had this statement been in effect when those costs were incurred.”

A32. The Board acknowledges that reporting entities have had numerous years to implement SFFAS 10 (as well as other standards). The fact remains some entities have not had or do not have systems that could provide the information necessary and the conditions remain that existed when many of these standards were issued. In regards to SFFAS 10, the Board considered certain unique aspects to this category of general PP&E that justify a similar treatment that was provided when SFFAS 10 was established. Specifically, the Board believes it would be cost-beneficial to allow prospective treatment of IUS because it typically has a shorter useful life than other assets and is a soft asset that is harder to inventory when compared to tangible assets. These facts make the cost of implementation higher than for other general PP&E and the benefit lower due to the shorter time the IUS would be reported as an asset that would be amortized to expenses.

A33. Therefore, the Board believes the most appropriate path is to amend the implementation guidance provided in SFFAS 10 to provide for prospective application of IUS if the reporting entity elects to do so. Considering some departments may be at different stages of auditability of component reporting entities and other factors that may need to be considered when implementing a Statement such as this, the Board determined that the Statement should provide flexibility. Therefore, the guidance was also updated to provide for an alternative valuation method of deemed cost that is consistent with general PP&E. Considering IUS are classified as general PP&E, the Board believes it appropriate to allow use of deemed cost and to refer users to the deemed cost implementation guidance in SFFAS 6. Together, these amendments allow the preparer to elect to report existing IUS based on deemed cost, to capitalize IUS prospectively, or to recognize IUS in development but not IUS in service.

Amendments to SFFAS 23, Eliminating the Category National Defense Property, Plant and Equipment

A34. The purpose of SFFAS 23 was to amend certain standards with regard to national defense (ND) PP&E. More specifically, SFFAS 23 rescinded the term “ND PP&E.”

A35. SFFAS 23 also provided implementation guidance for assets reclassified as general PP&E. Much of that guidance referred to the requirements in the implementation guidance provided in SFFAS 6. SFFAS 23 was effective for periods beginning after September 30, 2002, with earlier implementation encouraged. The Board believes it appropriate to rescind the implementation guidance in SFFAS 23 and refer users to the implementation guidance in SFFAS 6 that applies to all general PP&E, including general PP&E assets previously considered ND PP&E.

A36. By rescinding the paragraphs in SFFAS 23, the Board ensured the appropriate and pertinent guidance was included in the amendments to the SFFAS 6 Implementation Guidance. The Board chose not to rescind SFFAS 23 in its entirety because the standards provide other amendments, such as rescinding the term ND PP&E as discussed above, that must be maintained.

Rescission of SFFAS 35, Estimating the Historical Cost of General Property, Plant and Equipment: Amending Statements of Federal Accounting Standards 6 and 23

A37. The purpose of SFFAS 35 was to clarify that reasonable estimates of original transaction data historical cost may be used to value general PP&E. It was to establish a cost effective method to comply with SFFAS 6 by allowing reasonable estimates that were in accordance with SFFAS 6, as amended.

A38. As explained in SFFAS 35, basis for conclusion paragraph A12.:

The Board stresses to federal entities that the measurement basis for G-PP&E remains historical cost; however, reasonable estimates are allowed. The Board believes entities should use judgment regarding the decision to use estimated historical cost in lieu of original transaction based data. The Board also notes that estimates are widely used throughout the financial statements. In this case, estimates should provide a reasonable approximation of historical cost; the measurement basis required for G-PP&E.

A39. When SFFAS 35 was issued, the Board believed that allowing or encouraging estimates as reporting entities worked towards implementing systems and processes that could capture historical data would be beneficial. However, it appears that this has not occurred at all Departments, and the language in SFFAS 35 has often been misinterpreted to be something other than reasonable estimates that are in accordance with SFFAS 6.

A40. Therefore, the Board believes it appropriate to rescind SFFAS 35. The Board acknowledges that reasonable estimates are permitted in the preparation of financial statements, with or without the existence of SFFAS 35. As noted in paragraph A17. of SFFAS 35 : “Estimates that do not lead to material misstatements are acceptable without guidance from the Board.” However, the Board believes it would be clearer and not misinterpreted by users if SFFAS 35 was rescinded.

A41. While rescinding SFFAS 35 in its entirety, the Board ensured any pertinent guidance was included in the amendments to the SFFAS 6 Implementation Guidance.

DISCLOSURES

A42. The disclosures required are also included in the amendments to the implementation guidance in SFFAS 6 and 10. Specifically, the election to apply the provisions of this Statement should be disclosed in the financial statements in the first reporting period in which the reporting entity makes an unreserved assertion that its financial statements, or one or more line items addressed by this Statement, are presented fairly in accordance with GAAP. The first reporting period would be the first financial statement year end that an unreserved assertion is made. The Board does not believe this would include interim financial statements that presently are unaudited and do not include note disclosures.

A43. The Board notes that the term “unreserved assertion” may be used in other contexts. For example, certain entities’ management (such as DoD) may be required to make management assertions regarding its financial information and that DoD financial statements are validated as ready for audit by not later than September 30, 2017. This Statement refers to an unreserved assertion that the reporting entity’s “financial statements,

or one or more line items addressed by this Statement, are presented fairly in accordance with GAAP.” Other assertions – such as being ready for an audit - may or may not accompany such an assertion.

- A44. The reporting entity should also disclose a description of what valuation method(s) deemed cost is based on, but no disclosure of amounts valued at deemed cost is required.
- A45. A reporting entity electing to exclude land should disclose this fact in the first reporting period in which the reporting entity makes an unreserved assertion that its financial statements, or one or more line items are presented fairly in accordance with GAAP. In addition, those reporting entities electing to exclude land should also provide the number of acres of land held at the beginning of each reporting period, the number of acres added during the period, the number of acres disposed of during the period, the number of acres held at the end of each reporting period, and the number of acres for which an amount is included in general PP&E. The Board believes requiring these disclosures would meet accountability and ensure appropriate measures are continued for existence and completeness.
- A46. The disclosure requirements included in the amendments to SFFAS 10 are broader because the reporting entity may choose among alternatives for establishing an opening balance for internal use software. It provides for an alternative valuation method of deemed cost that is consistent with general PP&E and prospective application. A reporting entity electing to apply the alternative methods should disclose this fact and describe the alternatives used in the first reporting period in which the reporting entity makes an unreserved assertion that its financial statements, or one or more line items are presented fairly in accordance with GAAP. In the event different alternatives are applied by component reporting entities consolidated into a larger reporting entity, the alternative adopted by each significant component should be disclosed.

APPLICATION OF THIS STATEMENT

- A47. A component reporting entity that is in the process of implementing systems that are GAAP compliant is permitted to apply this Statement at the time it makes an unreserved assertion that its financial statements, or one or more line items addressed by this Statement, are presented fairly in accordance with GAAP. This Statement allows component reporting entities (for example, DoD components) to make the assertion at different times. The reporting entity may make the assertion after a sufficient number of components do so. This Statement considers the opening balances and subsequent transactions of these component reporting entities as deemed cost for the consolidated reporting entity when its assertion is made.
- A48. Using the DoD example, certain DoD components may have transitioned at an earlier date to GAAP compliant systems; this allows them to assert independently of the larger DoD. DoD would make a DoD-wide assertion when a sufficient number of DoD components are compliant. While a DoD component’s “deemed cost” opening balance might be earlier than the DoD-wide opening balance, the consolidation of the various methods would be DoD’s opening balance deemed cost at the beginning of the period DoD was able to make

an unreserved assertion on its financial statements or one or more line items addressed by this Statement.

A49. Considering the flexibility allowed with the Statement, reporting entities should ensure they are ready to make an unreserved assertion that their financial statements, or one or more line items addressed by this Statement, are fairly presented prior to making the election since it may only be made once. A complex entity should work with its components to ensure the most appropriate method allowed by this Statement is selected. Further, reporting entities should ensure issues such as supporting documentation for opening balances established are addressed and validated through sampling or other means, including consideration of any audit findings or conclusion affecting the reliability of the valuation, prior to making the unreserved assertion. The importance of a reporting entity being prepared to make the unreserved assertion is critical because the election may only be made once. For example, if a reporting entity makes an unreserved assertion regarding the FY 2018 beginning balances, the reporting entity must be able to support the valuation, in all material respects. If the audit for FY 2018 determines that the valuation does not comply with the alternative valuation in all material respects, the reporting entity then would need to:

- a. continue in subsequent years to correct or support the valuation as of the beginning of FY 2018, or
- b. accept a modified audit report until the reporting entity demonstrates compliance with SFFAS 6 (as amended), in all material respects.

A50. Reporting entities that meet the conditions specified in paragraph 5 and elect to apply the alternative valuation method in establishing opening balances permitted by this Statement are subject to the reporting requirements under paragraph 13 of Statement of Federal Financial Accounting Standards (SFFAS) 21: *Reporting Corrections of Errors and Changes in Accounting Principles*. Specifically, paragraph 12 of SFFAS 21 states "...For the purposes of this standard, changes in accounting principles also include those occasioned by the adoption of new federal financial accounting standards."

A51. Therefore, reporting entities meeting the conditions and electing to apply this Statement should follow the guidance in SFFAS 21 paragraph 13(a) – (c) for all changes in accounting principles:

- (a) The cumulative effect of the change on prior periods should be reported as a "change in accounting principle." The adjustment should be made to the beginning balance of cumulative results of operations in the statement of changes in net position for the period that the change is made.
- (b) Prior period financial statements presented for comparative purposes should be presented as previously reported; and
- (c) The nature of the changes in accounting principle and its effect on relevant balances should be disclosed in the current period. Financial statements of subsequent periods need not repeat the disclosure."

A52. SFFAS 21 provides that the adjustment should be made to the beginning balance of cumulative results of operations in the statement of changes in net position for the period that the change is made. Thus, no change would be made to the ending net position of the

previous year. The disclosures should be at a high level and explain that opening balances of a particular line item or group of line items were valued at deemed cost under this Statement, briefly describe deemed cost, and indicate the effect of adoption on beginning net position.

A53. In addition, alternative valuation methods provided in this Statement may be applied in correcting errors related to the opening balances discovered in later reporting periods if needed.

A54.

APPENDIX B: ABBREVIATIONS

DoD	Department of Defense
ED	Exposure Draft
FASAB	Federal Accounting Standards Advisory Board
GAAP	Generally Accepted Accounting Principles
IPSAS	International Public Sector Accounting Standards
IPSASB	International Public Sector Accounting Standards Board
IUS	Internal Use Software
PP&E	Property, Plant and Equipment
PRV	Plant Replacement Value
SFFAC	Statement of Federal Financial Accounting Concepts
SFFAS	Statement of Federal Financial Accounting Standards

APPENDIX C: GLOSSARY

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DoD Implementation Guidance Request Project History of Project and Board Decisions

August 2015

At the August Board meeting, the Board made decisions on issues regarding the Draft Statement, *Opening Balances for Inventory, Operating Materials and Supplies and Stockpile Materials*. The Board considered the comment letters received in response to the exposure draft, a summary of the issues, and recommendations proposed by FASAB staff. In addition, the Board discussed and agreed to several changes to the Draft Statement, *Opening Balances for Inventory, Operating Materials and Supplies and Stockpile Materials*. The Board will review editorial changes and expects to vote on the Statement before the next meeting.

In a separate request from DoD, the Board considered options regarding baseline estimates for all categories of general property, plant, and equipment (GPP&E). After considering the options regarding baseline estimates prepared by FASAB staff and also submitted by DoD, the Board tentatively agreed to the following:

- Allow deemed cost (estimated historical cost, fair value, or replacement cost) for all GPP&E.
- Provide prospective treatment for internal use software and land.
- Acres of land would be disclosed.

June 2015

The proposed Statement of Federal Financial Accounting Standards entitled *Opening Balances for Inventory, Operating Materials and Supplies (OM&S) and Stockpile Material* was released on June 2, 2015. The proposed Statement would allow a reporting entity to apply an alternative valuation method in establishing opening balances for inventory, OM&S, and stockpile materials. The alternative valuation method is available only when presenting information following generally accepted accounting principles (GAAP) either (1) for the first-time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP- based financial statements without use of the alternative valuation method. This Statement is effective for periods beginning after September 30, 2016. Earlier implementation is encouraged.

At the June 2015 Board meeting, the Board discussed DoD's request to clarify the treatment of capital improvements when estimating the historical cost of GPP&E. They indicated that separately identifying the cost of capital improvements would be costly and time consuming. The Board agreed that issuing a Statement and making the appropriate amendments to standards may provide a cost effective approach for DoD regarding baseline estimates of general property, plant, and equipment (GPP&E). While the Board did not decide on a particular approach, many options were discussed at the meeting and detailed in the minutes.

It was agreed that FASAB staff would work with DoD and facilitate meetings to gather input from their auditors to discuss the approaches further. Staff will also consider the issues related to all

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general property plant and equipment, including real property, military equipment and land so all items can be addressed in one Statement.

April 2015

The Board considered an exposure draft of a proposed Statement of Federal Financial Accounting Standards entitled *Opening Balances for Inventory, Operating Materials and Supplies (OM&S) and Stockpile Materials*. The proposal would permit the use of alternative methods in establishing opening balances for inventory, operating materials and supplies, and stockpile materials under SFFAS 3, *Accounting for Inventory and Related Property*. After reviewing and discussing the draft proposed standards the Board agreed to the proposal with primarily editorial changes. The exposure draft is being finalized and is expected to be released for comment in early June.

The Board discussed another draft document, exposure draft of an Interpretation of a Statement of Federal Financial Accounting Standards entitled *Interpretation of Statement of Federal Financial Accounting Standards (SFFAS) 6, Accounting for Property, Plant, and Equipment as amended by SFFAS 35, Estimating the Historical Cost of General Property, Plant, and Equipment: Amending Statements of Federal Financial Accounting Standards 6 and 23*. The objective is to clarify whether capital improvements are included when estimating the historical cost of general property plant and equipment (G-PP&E) and whether estimates are permitted to capture the historical cost of construction in progress. The Board generally agreed but requested clarification of the treatment of new capital improvements. The Board will discuss revisions at its June meeting.

February 2015

The Board was provided an update on the progress on the Department of Defense (DoD) Implementation Guidance Request project.

- In regards to the research and development area, staff held a kickoff meeting with DoD, but it was agreed that DoD was to assess whether FASAB assistance within the GAAP hierarchy is needed. However, FASAB staff will be a liaison with DoD FIAR working groups to assist on discrete issues. FASAB's role will be to assist if there is a need for GAAP guidance.
- It was agreed staff would consider the Board member comments regarding acceptable valuation methodologies for Inventory and Operating Materials & Supplies at transition to systems capable of accounting in accordance with SFFAS 3 when historical cost information is unavailable and develop a draft proposal for the Board's consideration at the April 2015 Board meeting. For example, the Board agreed that deemed cost should be written broadly or generically so that could be adapted to DoD. In addition, staff will consider broadening the scope (such as a first-time adopter standard and/or if it should be for all assets) and determine the best approach (standard, technical bulletin).

December 2014

The Board reviewed the DoD Implementation Guidance Request Project Plan and was provided an update on efforts to date from FASAB's contractor.

The Board did not make any decisions at the December 2014 meeting on this agenda item as this was an update. Important items discussed that are detailed in the minutes include the following:

- Staff anticipates making progress in the Research and Development area in the coming months contingent upon DoD providing contact information and more information about the request.
- The issue of “end user” will be researched further to determine how best to address it.
- Follow-up with the branches (as well with the Marines) will be held to confirm all results to date on the deployed assets issue. A final recommendation will be presented to the board for approval, vote and record in the minutes.
- FASAB staff (with contractor assistance) plans to continue research and gain more information in various areas as it relates to inventory—including reparables, principal items, and confirming our understanding of inventory accounting and valuation processes at each branch.
- FASAB staff plans to research various areas discussed by board members at the meeting such as IFRS 1, GASB 34, further analysis and consideration of turnover rates, etc. The members also suggested meeting with the DoD IG at a time deemed appropriate.