Federal Accounting Standards Advisory Board

October 11, 2012

Memorandum

To: Members of the Board

From: Melissa Loughan, Assistant Director

Wendy M. Payne

Through: Wendy M. Payne, Executive Director

Subj: **Federal Reporting Entity--Tab C**[1]

MEETING OBJECTIVES

- To approve a pre-ballot Exposure Draft (ED) for the Federal Reporting Entity project.

The objectives for the October Board meeting are to approve a pre-ballot ED. To accomplish this optimistic goal, the Board will be required to approve changes agreed upon at the last meeting, consider other suggested changes and vote on 4 areas, including the final related party language. These actions will enable staff to make any needed changes for additional deliberation or review at Thursday's meeting. This will allow staff to prepare a ballot ED for approval after the October meeting.

BRIEFING MATERIAL

The transmittal memorandum includes a discussion of issues and recommendations beginning on page 3 under Staff Analysis and Recommendations. A full list of Questions for the Board appears on the final page.

- Attachment 1: Pre-Ballot ED

You may electronically access all of the briefing material at http://www.fasab.gov/board-activities/meeting/briefing-materials/

441 G Street NW, Mailstop 6K17V, Washington, DC 20548 ♦(202) 512-7350 ♦fax 202 512-7366

BACKGROUND

As you may recall at the August meeting, the Board deliberated many issues in the proposed standard and agreed upon certain changes. Staff implemented those changes.

NEXT STEPS

The goal of completing the ED shortly after the October 2012 meeting is contingent upon the Board's decisions and extent of changes at this meeting and the Board's vote on the related party language and the revised language for the basis for conclusion to address the Federal Reserve System. It is important that any member intending to offer an alternative view state their intent.

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MEMBER FEEDBACK

If you require additional information or wish to suggest another alternative not considered in the staff proposal, please contact staff as soon as possible. In most cases, staff would be able to respond to your request for information and prepare to discuss your suggestions with the Board, as needed, in advance of the meeting. If you have any questions or comments prior to the meeting, please contact me by telephone at 202-512-5976 or by e-mail at loughanm@fasab.gov with a cc to paynew@fasab.gov.

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[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.

STAFF ANALYSIS AND RECOMMENDATIONS

1. Updated Exposure Draft for Decisions at the August Meeting & Other Changes

The goal of the session is to approve changes incorporated into the ED as well as identify any remaining member concerns with the ED. As you will see in the Marked Version of the ED, staff updated the document for the decisions made at the August meeting.

After considering the August minutes and transcripts carefully, staff incorporated into the ED agreed upon wording changes and suggested language revisions made by Board members during and following the August meeting.

For example, staff incorporated the following changes that were approved by the Board from Mr. Steinberg's Alternate Draft:

1. Revised key terminology by replacing the following: 'core' with 'consolidation' and 'non-core' with 'disclosure'
2. Added "organization" to the "relationship" objective for the disclosure relating to "disclosure entities"
3. Removed the enumerated disclosures tailored to and required for entities exercising powers reserved to the sovereign

In addition, staff added questions to respondents for (1) organizations with multiple funding sources (such as museums) and (2) intervention actions beyond the scope of the standard.

Further, staff also updated the Basis for Conclusions to reflect decisions made at recent meetings and to be consistent with other changes made in the document.

Certain changes staff wanted to point out to the Board as they relate to new language and may be considered beyond 'editorial' for the Board's consideration and approval.

Federal Reserve System BfC Language

Staff shared draft language after the August Board meeting regarding the Federal Reserve System and how consolidation might obscure the financial effects of fiscal policies. Staff received comments from approximately half of the members on the draft language. Members offered suggestions to the draft language for clarity.

Of those responding, certain members appeared to support the draft language, while certain members expressed some reservation with the draft language. Of the members noting concern, one member believed consolidation of the Federal Reserve was appropriate and any obscurity that may occur could be made clear through the notes to the financial statements. This same member commented that "Historically, 95% of FRBank interest earnings on US Treasuries and mortgage backed securities have been returned to the US Treasury at the end of the year. In effect purchases of US Treasuries by the FRBanks (and at the direction of the FOMC made up of a majority of the Board of Governors of the FRB – a federal entity) results in almost interest free loans to the federal government." The reporting of the FRB and FRBanks is a very important issue. This member also suggested that a project be added to address how activities of the Central Bank should be reported-- as consolidated with the federal government or as a stand –a-lone entity.

Another member believes, the Board is obligated to understand prior to issuing the standard how the Federal Reserve Board will be classified and reported upon. However, staff does not believe it is the Board's intent to explicitly state how any entity will be classified in the standard or basis for conclusion.

Based on the comments received, staff revised the basis for conclusions language as follows (See par. A31 - A35 in the ED for marked changes.) :

A1. Differences in purposes and governance structures by organizations may require differences in presentation of related financial information. This Statement provides that the reporting entity should first determine which organizations are to be included in the reports. Next the reporting entity should classify the included organizations between consolidation entities and disclosure entities.

A2. Different means of presenting relevant information are provided for consolidation and disclosure entities. The distinction between consolidation entities and disclosure entities is based on the degree to which the following characteristics are met: the entity is taxpayer supported, is governed by the Congress and/or the President, imposes or may impose risks and rewards on the taxpayer, and/or provides goods and services on a non-market basis. Maintaining a distinction between consolidation entities where accountability rests with the Congress and/or the President, and disclosure entities that are more financially (or operationally) independent will provide information to users that is more understandable and relevant. In some cases, disclosure of information regarding an individual entity is more useful than consolidation of the individual entity's financial statements in the government-wide financial statements. In other cases, consolidation of individual entities' financial statements is needed to provide fair presentation of activities financed by the taxpayers, accountable to the Congress and/or the President, and/or relying on the taxpayers to settle liabilities.

A3. The Board considered whether the proposed principle-based standards were likely to result in fair presentation of certain significant entities or classes of entities. For example, in considering the Federal Reserve System, some members believe that consolidation might obscure the financial effects of fiscal policies while disclosure might shed more light on monetary policy. However, one member believes consolidation of the Federal Reserve System is appropriate and any obscurity that may occur could be made clear through the notes to the financial statements. The Federal Reserve System is presently structured to facilitate monetary policy decisions that are independent of fiscal policy decisions by the President and Congress.

A4. Because monetary policy decisions are often executed through the purchase and sale of Treasury securities in the open market,[2] Treasury securities are a significant asset of the Federal Reserve Banks. If the Federal Reserve System is consolidated in the government-wide financial statements, any Treasury securities held as assets by the Federal Reserve System would be eliminated against the Treasury securities identified as liabilities. Accordingly, this use of Treasury securities to conduct monetary policy may introduce volatility and variability in the reported amount of Treasury securities outstanding unrelated to the fiscal policies of the federal government. Changes in these amounts arising from budgetary deficits and surpluses could be obscured by changes arising from monetary policy. In addition, liabilities for Federal Reserve notes outstanding and deposits by depository institutions would be reported on the consolidated balance sheet. These liabilities differ in character from liabilities arising from fiscal policy and may distort the government-wide financial statements.

A5. In contrast to consolidation, disclosures regarding the Federal Reserve System may aid users in understanding the Federal Reserve System, its relationship with the federal government, and any significant activities or risks posed to taxpayers. Principle-based standards do not result in the Board deliberating on the classification of the Federal Reserve System or any other specific entity. However, deliberations were conducted to assure the Board that the proposed standards were adequate and the elements of the standards were appropriate for application given the unique role of the central bank.

Question 1 for the Board:

Does the Board generally agree with the revised proposed language to address the Federal Reserve System and how consolidation might obscure the financial effects of fiscal policies? (Staff believes a Board <u>vote</u> is required.)

Control Definition

As you might recall, Mr. Steinberg's alternate version suggested a slight change to the control definition by revising it to "Control with <u>possible</u> benefits or risk of loss" versus the August ED wording of "Control with expected benefits of risk of loss."

Another member requested staff to switch the order of 'expected benefits' and 'risk of loss' because the member believed the federal government more often deals with risk of loss so that should be more prominent when considering the control definition. While both suggestions have merit exclusively, it was difficult for staff to incorporate both suggestions.

Therefore, staff proposes the following revision to the control definition (see par. 10 of the ED for marked changes.):

[2] The Federal Reserve Act, Section 14, authorizes Federal Reserve banks to buy and sell bonds and notes of the United States but requires when they exercise this authority and purchase or sell Treasury Securities, it must be done in the open market (rather than directly from or to the Treasury).

Control with risk of loss or expectation of benefit "Control with risk of loss or expectation of benefit" is the power to impose will on and/or govern the financial and/or operating policies of another organization with the potential to be obligated to provide financial support or assume financial obligations or to obtain financial resources or non-financial benefits.

Question 2: for the Board:

Does the Board generally agree with the revisions to the control definition? (Staff believes a Board vote is required.)

There were other changes incorporated into the ED, either suggested by Board members or staff and staff believed improved the document. Most were minor or editorial in nature and don't warrant an explanation in this memo and staff did not believe they would require a vote by the Board.

Question 3 for the Board:

Does the Board have any questions or comments on any of the other proposed changes referenced above or on any of the ones noted throughout the ED?

2. Related Party Language

At the August meeting, the Board considered a draft that relied heavily on listing parties to be included and excluded. In addition, the proposal provided room for judgment by incorporating a misleading to exclude provision. While the Board did not have a formal vote on the language at the August meeting, it did appear there was general agreement with the direction.

The Board provided staff with suggestions—such as to move the notion of misleading to exclude so it was more prominent in the language to guide preparers. The Board also suggested that the ED provide examples of special interest groups. One member also suggested that a question to respondents be considered so the Board could gather additional information if there are other organizations that should be excluded from related party reporting to better ensure there are no unintended consequences. Staff incorporated these and other suggestions by members.

Based on the feedback at the August meeting, staff revised the Related Party language as follows (See par. 74- 83 in the ED for marked changes.):

Related Party

1. In addition to entities for which Congress and the President are accountable[3], the federal government may have the ability to exercise significant influence over other organizations in making financial and operating decisions or to be influenced by its relationship with the other organizations. Such relationships are numerous and not all warrant disclosure. Guidance is provided below but judgment will also be required to identify relationships that warrant disclosure as related parties.

2. **Related parties** are not controlled or owned by the federal government. Organizations are considered to be related parties if the existing relationship[4] or one party to the existing relationship has the ability to exercise significant influence over the other party in making financial and operating decisions.

3. Significant influence (for the purpose of this Statement) is the power to participate in the financial and operating policy decisions of an entity, but not control those policies. Significant influence may be exercised in several ways, sometimes by representation on the board of directors or equivalent governing body but also by, for example, participation in the policy making process, interchange of managerial personnel, or dependence on technical information. Significant influence may be gained by an ownership interest, statute, or agreement.

4. Significant influence does not arise from regulatory actions or economic dependency alone. However, regulation or economic dependency, together with other factors, may

[3] Entities for which the Congress and President are accountable are in the budget, owned, or controlled and would meet the inclusion principles and be reported as either a consolidation or disclosure entity and not be subject to related party reporting.
[4] Relationship as used in this context refers to material transactions or events involving both parties.

give rise to significant influence and therefore a related party relationship. Judgment is required in assessing the impact of regulation and economic dependence on a relationship.

5. Although significant influence exists among the component reporting entities of the federal government, component reporting entities are subject to the overall direction and operate together to achieve the policies of the federal government and are not considered related parties. Therefore, component reporting entities need not be disclosed as related parties by other component reporting entities.

6. Further, in the context of this Statement, related parties are organizations with the ability to exercise significant influence –financially and operationally – such that it would be misleading to exclude disclosures regarding the relationship. Related parties *generally* would include but are not limited to:

   a. Government sponsored enterprises not meeting the Inclusion Principles

   b. Organizations governed by representatives from each of the governments that created the organization, including the United States, wherein the federal government has agreed to ongoing or contingent financial support to accomplish shared objectives (for example, multi-lateral development banks)

7. In the context of this Statement, the following *generally* would not be considered related parties:

   a. Entities meeting the Inclusion Principles

   b. Organizations with which the federal government transacts a significant volume of business resulting in economic dependence such as government contractors, state and local governments, collegial institutions and non-profit organizations

   c. Key executives

   d. Organizations owned or managed by key executives, other employees, or members of their families

   e. Component reporting entities of the federal government (see full discussion in par. 5)

   f. Foreign governments

   g. Organizations created through treaties or trade agreements that define common goals and means for joint action where the U.S. role in governing and financing the organizations is not significant

   h. Special interest groups[5]

[5] Special Interest groups refers broadly to organizations whose members share common concerns and try to influence government policies. Examples include but are not limited to International Brotherhood of

8. Although par. 7 *generally* permits the exclusion of certain organziations as related parties, other factors may create a need for related party reporting and disclosures. The use of judgment will be necessary in identifying those factors consistent with the information needs described in par 9.

9. Certain information regarding related party relationships may enable users to better understand the financial statements of the reporting entity because:

   - Related party relationships might expose the federal government to risks or provide opportunities that would not have existed in the absence of the relationship;

   - Related party relationships can influence the way in which the federal government operates with other entities in achieving its individual objectives; and

   - Related parties may enter into transactions that unrelated parties would not enter into, or may agree to transactions on different terms and conditions than those that would normally be available to unrelated parties.

10. For any Related Party, the following should be disclosed:

   - Nature of the federal government's relationship with the entity, including the name of the entity or if aggregated, a description of the related parties. Such information also would include as appropriate: the percentage of ownership interest.

   - Other information that would provide an understanding of the relationship and potential financial reporting impact, including financial-related exposures to potential gain and risk of loss to the reporting entity resulting from the relationship.

Question 4 for the Board:

Does the Board generally agree with the proposed Related Party language and disclosure requirements? (Staff believes a Board vote is required.)

Teamsters, American Public Power Association, Christian Coalition, the National Organization for Women (NOW) and the National Rifle Association (NRA)

3. ***Title of the Document***

An issue that projects often revisit is the title of the final document. The title of the federal reporting entity project has been difficult to pin down due to the scope. The current title "Identifying and Reporting upon Organizations to Include in General Purpose Federal Financial Report" appears to be grammatically challenged.

Further, when the Board last discussed the title it acknowledged there were still open issues and therefore may still require revising. Considering we are at the point of a pre-ballot, staff believes it was time to consider the title one last time, especially considering some of the recent changes in terminology.

Staff proposes the following titles for the Board's consideration:

1. **Identifying Organizations to Include in General Purpose Federal Financial Reports and Related Presentation Requirements**

2. **Identifying and Presenting Information about Organizations in General Purpose Federal Financial Reports**

3. **Including and Reporting Organizations in General Purpose Federal Financial Reports**

4. **Identifying Organizations to Include and Report in General Purpose Federal Financial Reports**

5. **Reporting Entities and Related Parties**

Staff believes the first option "Identifying Organizations to Include in GPFFR and Related Presentation Requirements" is the *best option* because it describes the scope of the Statement. Staff also believes this most closely describes the approach taken in the statement—identifying organizations to include in the general purpose federal financial reports and presentation requirements. Staff believes this is consistent with the purpose requirements as presented in par. 2 and the scope presented in par. 6 of the ED.

If the Board would prefer a much more concise alternative staff would recommend one of the shorter alternatives presented above.

However, staff believes the first option appears to be the best aligned title with the ED as currently written.

Question 5 for the Board:

Does the Board agree with the staff recommended title for the ED "Identifying Organizations to Include in General Purpose Federal Financial Reports and Related Presentation Requirements?" (Staff believes a Board vote is required.)

Question 6 for the Board:

Does the Board wish to bring up any technical issues or concerns that should be addressed before moving toward a ballot draft?

QUESTIONS FOR THE BOARD

1. **Does the Board generally agree with the revised proposed language to address the Federal Reserve System and how consolidation might obscure the financial effects of fiscal policies?**

2. **Does the Board generally agree with the slight revisions to the control definition?**

3. **Does the Board have any questions or comments on any of the other proposed changes referenced above or on any of the ones noted throughout the ED?**

4. **Does the Board generally agree with the proposed Related Party language and disclosure requirements?**

5. **Does the Board agree with the staff recommended title for the ED "Identifying Organizations to Include in General Purpose Federal Financial Reports and Related Presentation Requirements?"**

6. **Does the Board wish to bring up any technical issues or concerns that should be addressed before moving toward a ballot draft?**

Federal Accounting Standards Advisory Board

Identifying Organizations to Include in General Purpose Federal Financial Reports and Related Presentation Requirements

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Statement of Federal Financial Accounting Standards

Exposure Draft

Written comments are requested by Date 90 days after issuance

Month Date, 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 to comment, or preliminary views document may be issued before an exposure draft is released 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.

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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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FASAB

Federal Accounting Standards Advisory Board

September 30, 2012

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, *Identifying Organizations to Include in GPFFR and Related Presentation Requirements* are requested. Specific questions for your consideration appear on pages 9-13 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 January 25, 2013.

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 email 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. A public hearing has been scheduled at 9:00 AM on February 27, 2013, in Room 7C13 at the GAO Building, 441 G Street, NW, Washington, D.C.

Tom L. Allen

Chairman

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Executive Summary

What is the Board proposing?

The Board is proposing principles to ensure information about organizations for which elected officials are accountable is reported in general purpose federal financial reports (GPFFR). The principles proposed to guide financial reporting recognize the complex tools available to and used by elected officials to address public policy challenges. Those tools include the ability to create organizations with varying legal designations (for example, government agencies, not-for-profit organizations, corporations) and differing degrees of autonomy. The principles herein are not intended to establish whether an entity is or should be considered a federal agency for legal or political purposes. Rather, this exposure draft (ED) provides principles to guide preparers in determining what organizations are required to be included in the reporting entity's GPFFR for financial accountability purposes.

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The government-wide GPFFR should include all organizations (1) budgeted for by federally-elected officials of the federal government, (2) owned by the federal government, and (3) controlled by the federal government with the risk of loss or the expectation of benefits. When one of these three conditions exists, the Board believes certain information regarding the organization is necessary to provide accountability.

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This ED also provides criteria for determining the most appropriate means to present information about these organizations. Consolidated financial statements presenting the financial position and results of operations for those organizations financed by the taxpayer, governed directly by elected or appointed officials, and/or relying on the taxpayer to settle liabilities are appropriate. Consolidated financial statements present the financial information as if the organizations were a single economic entity. Such a presentation is needed to show – in aggregate – the net cost financed by the taxpayers and the assets available for use and the liabilities to be settled in the future. Organizations to be included in the consolidated financial statements within the GPFFR are referred to as "consolidation entities."

Consolidation is not appropriate for organizations operating with a high degree of autonomy. Some organizations that meet the principles for inclusion are insulated from political influence and intended to be non-taxpayer funded. Presenting information about these discrete organizations in consolidated financial statements would obscure the operating results and financial position of the organizations. Instead, information about these types of organizations should be disclosed in notes to the consolidated financial statements so that the nature of the relationship, relevant activity during the reporting period, and future exposures to risks and rewards are revealed. Organizations to be disclosed in GPFFR are referred to as "disclosure entities."

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The Board proposes each component reporting entity include all organizations for which it is accountable; that includes all consolidation and disclosure entities administratively assigned to it.

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The Board proposes related parties be disclosed if one party to an established relationship has the ability to exercise significant influence over the other party in making financial and operating decisions.

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The proposed Statement would be effective for periods beginning after September 30, 2015. Earlier implementation is encouraged.

How would this proposal improve federal financial reporting and contribute to meeting the federal financial reporting objectives?

This Statement would improve federal financial reporting by identifying organizations that should be included in the financial reports of the government-wide reporting entity and component reporting entities. This will provide users of GPFFR with comprehensive financial information about federal reporting entities and relevant activities and relationships to meet federal financial reporting objectives.

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In meeting the *Objectives of Federal Financial Reporting*, identifying the organizations for inclusion in the government-wide reporting entity and component reporting entities is critical to creating transparent reports to support accountability. As a democracy, elected officials are to be held accountable to the public and financial statements provide a means of doing so. In order to achieve accountability, the content and structure of the financial reports should be clear, complete and comprehensible to citizens.

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Questions for Respondents

The FASAB 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.

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.

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 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 electronically, please fax your responses to (202) 512-7366 and follow up by mailing 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 January 25, 2013.

Q1. The Board is proposing three inclusion principles for an organization to be included in the government-wide report:

- An organization with an account or accounts listed in the *Budget of the United States Government: Analytical Perspectives- Supplemental Materials* schedule *Federal Programs by Agency and Account* unless the organization is a non-federal organization receiving federal financial assistance
- When the federal government holds a majority ownership interest
- An organization that is controlled by the federal government with the risk of loss or the expectation of benefit

In addition, the Board is proposing that an organization be included in the government-wide report if it would be misleading to exclude it even though it does not meet one of the three inclusion principles.

Refer to paragraphs 18-33 of the proposed standards and paragraphs A13- A30 in Appendix A - Basis for Conclusions for a discussion and related explanation.

a. Do you agree or disagree with each of the inclusion principles? Please provide the rationale for your answer.

b. Do you believe the inclusion principles, and related definitions and indicators, are helpful and clear? Please provide the rationale for your answer.

c. Do you agree or disagree with the addition of a *Misleading to Exclude principle*? Please provide the rationale for your answer.

Q2. The Board proposes distinguishing between two types of entities in general purpose federal financial reports and that distinction ultimately determines how they are reported: consolidation entities and disclosure entities. Consolidation entities are (1) generally taxpayer supported as evidenced by their inclusion in the budget, (2) being governed by the Congress and/or the President, (3) imposing or may impose risks and rewards on the taxpayer, and/or (4) providing goods and services on a non-market basis. In contrast, disclosure entities are those that (1) receive limited or no taxpayer support, (2) have less direct involvement, and influence, by the Congress and/or the President, (3) are more likely to provide market based goods and services, and/or (4) impose limited risks and rewards on the taxpayers.

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Comment [ML1]: From this point forward—the change to consolidation and disclosure entities is not marked in the document.

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The Board proposes consolidation entities be consolidated in the government-wide financial statements. The Board proposes that information about disclosure entities be disclosed in notes to the government-wide financial statements. The Statement allows flexibility in the information presented as long as the disclosure objectives are met.

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Refer to paragraphs 35- 50 and 61-73 of the proposed standards and paragraphs,A31-A52, A60- A62 and A68-A77 in Appendix A - Basis for Conclusions for a discussion and related explanation.

a. **Do you agree or disagree there is a need to distinguish between consolidation and disclosure entities? Please provide the rationale for your answer.**

b. **Do you agree or disagree with the attributes used to make the distinction between consolidation and disclosure entities? Please provide the rationale for your answer.**

c. **Do you agree or disagree with the requirements for reporting on consolidation and disclosure entities? Please provide the rationale for your answer.**

Q3. For consolidation entities, the Statement would require consolidation of FASAB and FASB based information without conversion.

Refer to paragraph 62- 63 of the proposed standards and paragraphs A63-A67 in Appendix A - Basis for Conclusions for a discussion and related explanation.

Do you agree or disagree with the above referenced requirement? Please provide the rationale for your answers.

Q4. The Board proposes each component reporting entity report in its GPFFR organizations for which it is accountable; that includes consolidation entities and disclosure entities administratively assigned to it. Administrative assignments can be identified by evaluating: the scope of the budget process, whether accountability is established within a component reporting entity, and in rare cases, there may be instances of other significant relationships such that it may be misleading to exclude and/or misleading to include an organization not administratively assigned based on the previous principles.

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Refer to paragraphs 51-60 of the proposed standards and paragraphs A53-A59 in Appendix A - Basis for Conclusions for a discussion and related explanation.

Do you agree or disagree with the above referenced requirement? Please provide the rationale for your answers.

Q5. The Statement describes common types of disclosure entities to assist in identifying such entities. One common type is federal government intervention actions where ownership or control is expected to be other than permanent. The federal government may also have intervention activities (such as through extending loans or loan guarantees) that do not lead to organizations meeting the inclusion principles established in this Statement. Such transactions should be accounted for in accordance with the appropriate accounting standards per the GAAP hierarchy and this Statement does not include additional disclosure requirements for such intervention actions. Some believe disclosure requirements for all intervention actions should be addressed in this Statement.

Refer to paragraphs 47-50 of the proposed standards and paragraphs A50 in Appendix A - Basis for Conclusions for a discussion and related explanation.

Do you agree or disagree with the above referenced requirement? Please provide the rationale for your answers.

Q6. The Statement provides for all consolidation entities (and component reporting entities) to consider all organizations (which include funds) for which it is accountable. For certain organizations, such as museums, this may include consolidating funds from different sources—appropriated and donated funds.

Refer to paragraphs 51-60 of the proposed standards and paragraphs A20 in Appendix A - Basis for Conclusions for a discussion and related explanation.

Do you agree or disagree with the above referenced requirement? Please provide the rationale for your answers.

Q7. SFFAC 2 identified certain entities or types of entities (the Federal Reserve System, Government Sponsored Enterprises and Bailout Entities) that should not be considered part of the government-wide reporting entity. The Board is proposing new principles that should be applied to the entities previously excluded and conclusions reached to consider whether the entities are included in the general purpose federal financial reports. If a previously excluded entity is to be included based on these principles, principles are proposed to decide whether the entity is a consolidation or disclosure entity. These decisions would affect whether or how such entities are

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included in the general purpose federal financial reports. SFFAC 2 is being amended to remove these specific provisions.

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Refer to paragraph A85 in Appendix A - Basis for Conclusions for a discussion and related explanation.

Do you agree or disagree these amendments to SFFAC 2? Please provide the rationale for your answer.

Q8. The Board proposes related parties be disclosed if one party to an existing relationship has the ability to exercise significant influence over the other party in making financial and operating decisions. The Statement provides related parties are organizations of such significance that it would be misleading to exclude the organization and also provides a list of organizations that are generally excluded.

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Refer to paragraphs 74 -83 of the proposed standards and paragraphs A78-A81 in Appendix A – Basis for Conclusions for a discussion and related explanation.

a. Do you agree or disagree with the related party definition and requirements? Please provide the rationale for your answer.

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b. Do you agree or disagree with the list of exclusions? Please provide the rationale for your answer.

c. Are there additional exclusions that should be considered? Please provide the rationale for your answer.

d. Are there additional related party examples that should be included? Please provide the rationale for your answer.

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Q9. The Board proposes conforming changes to SFFAC 2 to rescind or amend language to move criteria for determining what organizations are required to be included in the federal reporting entity's GPFFR from a concepts statement to a standards statement

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Refer to paragraphs 84-98 of the proposed standards and paragraphs A82-A85 in Appendix A - Basis for Conclusions for a discussion and related explanation.

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Do you agree or disagree with the amendments? Please provide the rationale for your answer.

Q10. The Board proposes the Statement and Amendments to SFFAC 2, *Entity and Display* have an effective date of periods beginning after September 30, 2015.

Do you agree or disagree with this effective date? Please provide the rationale for your answer.

Q11. The Statement provides two non-authoritative appendices to assist users in the application of the proposed standards. The Flowchart at Appendix B is a tool that can be used in applying the principles established. The Illustrations at Appendix C offer hypothetical examples that may be useful in understanding the application of the standards.

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Refer to Appendix B-Flowchart and Appendix C-Illustration for the full explanation.

a. Do you agree the appendices are helpful in the application of the proposed standards?

b. Do you believe the appendices should remain after the Statement is issued?

Q12. Are there other unique situations that should be addressed within this Statement? Please explain fully and also how the situation is not addressed by this Statement when considered in its entirety.

Introduction

Purpose

1. The federal government and its relationships with organizations have become increasingly complex. Notwithstanding these complexities, general purpose federal financial reports (GPFFR) for the government-wide reporting entity should be broad enough to report the Congress and/or the President's accountability for those organizations. In addition, component reporting entity financial reports should allow the Congress and the President to hold management accountable for implementation of public policy decisions. Although Statement of Federal Financial Accounting Concepts (SFFAC) 2, *Entity and Display*, addresses identifying reporting entities and criteria for including components in a reporting entity, questions have continued in this area indicating the need for standards.[3] Standards that can be used to identify organizations to include in the GPFFR of the government-wide reporting entity and each component reporting entity are important to meeting federal financial reporting objectives.

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2. This Statement guides preparers of GPFFRs in determining what organizations to report upon, whether such entities are considered 'consolidation entities' or 'disclosure entities',[4] and what information should be presented. This guidance will ensure that users of GPFFRs are provided with comprehensive financial information about federal reporting entities and their relationships so that federal financial reporting objectives are met.

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3. The guidance recognizes the substance of the relationship between the federal government and an organization may not be reflected by an organization's legal form. As such, the legal form or designation of an organization does not always determine whether it should be reported in the government-wide GPFFR. Even in cases where legislation indicates an organization is "not an agency or instrumentality" of the federal government, the organization should be assessed against the guidance contained in this Statement to determine whether it should be included in the reporting entity's GPFFR. Inclusion results from a need for accountability given the nature of the relationship between the federal government and the organization but inclusion does not change the legal form of the organization.

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[3] SFFAC 2 is a Concepts Statement and is considered Other Accounting Literature. See SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles (GAAP) Including the Application of Standards Issued by FASB* for more information regarding the hierarchy.

[4] The distinction between consolidation entities and disclosure entities is based on the degrees to which the entity is (1) supported by taxpayers, (2) governed by elected or appointed officials, and (3) imposing risks on the taxpayer. See par. 34 - 50 for information.

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Materiality

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

Proposed Standards

Scope and Applicability

5. This Statement applies to federal entities that prepare **general purpose federal financial reports** (GPFFR) in conformance with generally accepted accounting principles (GAAP) as defined by paragraphs 5 through 8 of Statement of Federal Financial Accounting Standards (SFFAS) 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*. Paragraph 63 of this Statement applies to federal entities that prepare GPFFR in conformance with GAAP as provided by paragraphs 9 through 12 of SFFAS 34.

6. This Statement does not require any entity to prepare and issue GPFFRs. The purpose of this Statement is to enable entities preparing and issuing GPFFRs to determine:

   a. whether SFFAS 34 is applicable to an organization,

   b. what organizations should be reported on in the GPFFR of entities applying SFFAS 34,

   c. the manner in which information should be presented for organizations reported in the GPFFR, and

   d. what, **disclosures**, if any, are needed regarding related parties.

Definitions

Definitions in paragraphs 7 through 10 are presented within the standards because they are new terms intended to have a specific meaning when applying the standards. Terms shown in boldface type the first time they appear in the remainder of this document are presented in the Glossary at Appendix D with their existing definitions. Respondents to this proposal may want to examine all definitions before reviewing the Statement and Basis for Conclusions.

7. **Reporting Entity** Reporting entities are entities that issue a GPFFR because either there is a statutory or administrative requirement to prepare a GPFFR or they choose to prepare one. The term "reporting entity" may refer to either the government-wide reporting entity or a component reporting entity (see definitions below).

Statement of Federal Financial Accounting Concepts (SFFAC) 2 provides criteria for an entity to be a reporting entity.[5] The criteria focus on whether an entity should issue GPFFRs and are that a reporting entity's:

a. management is responsible for controlling and deploying resources, producing outputs and outcomes, and executing the budget or a portion thereof (assuming that the entity is included in the budget), and is held accountable for the entity's performance.

b. financial statements would provide a meaningful representation of operations and financial condition.

c. financial information could be used by interested parties to help them make resource allocation and other decisions and hold the entity accountable.

8. **Government-wide Reporting Entity** The government-wide reporting entity's GPFFR includes all organizations for which the Congress and/or the President are accountable based on principles established in this Statement.

9. **Component Reporting Entity** "Component reporting entity" is used broadly to refer to a reporting entity within a larger reporting entity.[6] Examples of component reporting entities include entities such as executive departments, independent agencies, government corporations, legislative agencies, and federal courts. Component reporting entities would also include sub-components (those components included in the GPFFR of a larger reporting entity) that may themselves prepare GPFFRs. One example is a bureau that is within a larger department that prepares its own standalone GPFFR.

10. **Control with risk of loss or expectation of benefit** "Control with risk of loss or expectation of benefit" is the power to impose will on and/or govern the financial and/or operating policies of another organization with the potential to be

[5] SFFAC 2, par. 29-37, provides a discussion on Identifying the Reporting Entity for General Purpose Financial Reporting.
[6] The larger reporting entity could be the government-wide reporting entity or another component reporting entity.

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Deleted: with expected benefits or risk of loss obligated to provide financial support or assume financial obligations or to obtain financial resources or non-financial benefits.[7] See paragraphs 22 - 31.

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Organizational Approach to Defining Boundaries

11. The federal government is unique because its constitutionally established powers, motivations, and functions are different from those of all other organizations. It is an extremely complex organization responsible for the common defense and general welfare of the nation. Although there are other perspectives,[8] such as a program perspective, an organizational approach was established in SFFAC 2[9] as the most appropriate perspective for understanding the composition of the federal government. SFFAC 2 established that GPFFRs should include the aggregation of organizations, which may be a fund, for which the federal government is financially accountable as well as other organizations for which the nature and significance of their relationship with the government are such that their exclusion would cause the federal government's financial statements to be misleading or incomplete.

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12. Accountability demands comprehensive reporting. To provide comprehensive reporting, the federal government must report on component reporting entities that serve varied purposes and have complex governance structures and finances. For example, certain distinctions must be maintained for financial reports to meet the reporting objectives established in SFFAC 1. In such cases, disclosures about the organization rather than financial information consolidated across all organizations may better meet these objectives.

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13. This Statement first establishes the principles for including organizations in the government-wide GPFFR (see Principles for Inclusion in the Government-wide GPFFR) then distinguishes between Consolidation Entities and Disclosure Entities (see section ' Reporting on Organizations – Consolidation or Disclosure').

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14. This Statement also establishes that component reporting entities must identify all consolidation and disclosure entities for which they are accountable so that both the component reporting entity and government-wide GPFFRs are complete.

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[7] For example, a non-financial benefit would be one where the federal government benefits from a service being provided to it or on its behalf.
[8] SFFAC 2, par. 13-28 discusses the budget and program perspectives of the federal government, as well as the intertwining of the perspectives.
[9] SFFAC 2, par. 31-38.

15. The Statement addresses presentation of financial information based on those decisions (see GPFFR- Consolidation and Disclosure).

16. Lastly the Statement provides for disclosure of related party relationships of significant influence that would misleading to exclude.

Principles for Inclusion in the Government-wide GPFFR

17. This Statement provides three principles for determining which organizations or funds should be included[11] in the government-wide GPFFR and also requires inclusion of organizations if it would be misleading to exclude them (see par. 33).

18. An organization[12] meeting any one of the three principles below is included in the government-wide GPFFR:

   a. In the Budget

   b. Majority Ownership Interest

   c. Control with Risk of Loss or Expectation of Benefit

In the Budget

19. An organization with an account or accounts listed in the *Budget of the United States Government: Analytical Perspectives- Supplemental Materials* schedule *Federal Programs by Agency and Account* should be included in the government-wide GPFFR unless it is a non-federal organization receiving federal financial assistance.[13] Any listed non-federal organizations receiving federal financial assistance should be assessed against the next two principles (*Majority Ownership Interest* and *Control with Risk of Loss or Expectation of Benefit*) to determine whether they should be included in the government-wide GPFFR.

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[11] 'Included' means the information is either consolidated or disclosed.
[12] Organization is used broadly to encompass organizations and funds in this Statement.
[13] As defined by the Single Audit Act Amendments of 1996, federal financial assistance is assistance that non-federal organizations receive or administer in the form of grants, loans, loan guarantees, property, cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, or other assistance.

Majority Ownership Interest

20. The federal government (directly or through its components) may have an ownership interest[14] in an organization. An ownership interest is a legal claim on the net residual assets of an organization such as holding shares or other formal equity instruments. The holding of an ownership interest usually but not always entitles the holder to an interest in voting rights.

21. Majority ownership interest exists with over 50% of the voting rights or net residual assets[15] of an organization. When the federal government (directly or through its components) holds a majority ownership interest in an organization it should be included in the government-wide GPFFR.[16]

Control with Risk of Loss or Expectation of Benefit

22. An organization that is controlled by the federal government with risk of loss or expectation of benefit should be included in the government-wide GPFFR. For these purposes, control with risk of loss or expectation of benefit is defined as follows:

    Control with risk of loss or expectation of benefit is the power to impose will on and/or govern the financial and/or operating policies of another organization with the potential to be obligated to provide financial support or assume financial obligations or obtain financial resources or non-financial[17] benefits. Both the power and either the risk of loss or expectation of benefits aspects of the definition should be met to justify inclusion of an organization. Hereafter, control with risk of loss or expectation of benefit is referred to as "control."

23. Control refers to the ability to control, whether or not that ability is actively exercised, and should be assessed at the reporting date regardless of the federal

[14] 'Ownership interest' is the possession of substantially all of the benefits and risks incident to ownership. *FASAB Glossary FASAB Pronouncements as Amended as of June 30, 2011.*
[15] For example, the federal government may hold more equity in preferred stock than all other stockholders but the preferred stock may be non-voting.
[16] Ownership interests 50% or less should be accounted for in accordance with the appropriate accounting standards per the GAAP hierarchy. However, the organization should still be assessed against the control inclusion principle and the misleading to exclude principle.
[17] For example, a non-financial benefit would arise when the federal government receives a service or a service is provided to others on its behalf.

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Deleted: with expected benefits or risk of loss government's ability to change it in the future. In determining whether control exists, it is necessary to determine the substance of the relationship between the federal government and the organization as it may not be completely reflected by the legal form of the relationship.

24. Control does not necessarily mean the federal government has responsibility for the management of the day-to-day operations of an organization. Rather, it is the federal government's authority to determine or influence the policies governing those activities that indicates control.

25. Determining whether control exists requires the application of professional judgment. The federal government achieves its objectives through a wide range of organizations which individually will fall on a continuum. At one end of the continuum, it is clear that an organization does not have the power to act independently and is controlled by the federal government—such as an executive department. At the other end, the organization has the power to act independently and, while the federal government may have a level of influence, it is clear that it does not have control—such as a foreign government.

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Indicators of Control

26. As discussed in the following paragraphs, there are indicators that should be considered in determining whether the federal government controls an organization. As noted above, consideration needs to be given to the nature of the relationship between the federal government and the organization and judgment applied to determine whether control exists.

27. Certain individual indicators provide persuasive evidence that control exists. Because each indicator provides strong evidence of control, meeting any one indicator would generally mean control is present. These indicators are when the federal government has the unilateral authority to:

    a. establish or amend the fundamental purpose and mission of the organization,[18] which may include authorizing the organization to exercise sovereign powers of the federal government and requiring the organization to carry out federal missions and objectives;

[18] Congressionally chartered nonprofit organizations identified under Title 36, Subtitle II and III, should not be considered controlled solely because amendments to their federal charter must be enacted through legislation. Instead, such organizations should be considered controlled only if they meet the indicators in paragraph 28 or another indicator in this paragraph.

b. appoint or remove a majority of the governing board members;

c. direct the governing body regarding the establishment and subsequent revision of financial and operating policies of the organization; or

d. dissolve the organization thereby having access to the assets and responsibility for the obligations.

28. Other indicators provide evidence that control exists, but must be considered in the aggregate and often require the application of professional judgment in assessing. These indicators are when the federal government has the ability to or is obligated to:

a. provide significant input into the appointment of members of the governing body of the organization or being involved in the appointment or removal of a significant number of members;

b. direct the ongoing use of the organization's assets;

c. direct investment decisions including to liquidate investments;

d. appoint or remove key executives or personnel;

e. approve the budgets or business plans for the organization;

f. require audits;

g. veto, overrule, or modify governing board decisions or otherwise significantly influence normal operations;

h. finance the deficits of, provide financial support to, or settle liabilities of the organization;

i. direct the organization to work with the government to provide services to taxpayers which may include determining the outcome or disposition of matters affecting the recipients of services;

j. establish, rescind, or amend the organization's governance framework;

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k. establish limits or restrictions on borrowing and investments of the organization; or

l. restrict the capacity to generate revenue of the organization, especially the sources of revenue.

Situations Where Control Does Not Exist

29. Because of the uniqueness of the federal government, control should not be inferred from either:

    a. authority to exercise regulatory powers over an organization; or

    b. economic dependency of the organization on the federal government.

30. The federal government has the power to regulate many organizations by use of its sovereign and legislative powers. For example, the federal government has the power to regulate the behavior of organizations by imposing conditions or sanctions on their operations. However, the governing bodies of the regulated organizations make decisions within the regulatory framework. Regulatory powers do not constitute control for purposes of this Statement because the federal government's interest in these organizations extends only to the regulatory aspects of the operations.

31. Certain organizations may be economically dependent on the federal government but ultimately retain discretion as to whether to accept funding or do business with the federal government. For example, many nonprofit organizations rely on federal government funding but that does not mean they are controlled by the federal government. Although the federal government may be able to influence organizations dependent on federal funding or business through purchasing power, the federal government typically does not govern their financial and operating policies.

Misleading to Exclude Principle

32. There may be instances when an organization does not meet the inclusion principles in paragraphs 18 through 28 yet the government-wide GPFFR would be misleading or incomplete if the organization were excluded.[19]

33. Organizations should be included in the government-wide GPFFR if it would be misleading to exclude them.

[19] Although such situations would be rare, this Statement provides for situations that may arise.

Reporting on Organizations--Consolidation or Disclosure

34. The principles above should be used to assess which organizations to include in GPFFRs. Next, a distinction should be made between "consolidation entities" and "disclosure entities" and that distinction ultimately determines how the organizations will be reported. This distinction is based on an assessment of the degree to which the following characteristics are met: the organization is taxpayer supported, is governed by the Congress and/or the President, imposes or may impose risks and rewards on the taxpayer, and/or provides goods and services on a non-market basis. Note, however, not all characteristics are required to be met to the same degree; classification is based on the assessment as a whole.

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Consolidation Entities

35. Entities which are financed primarily through taxes, fees, and other non-exchange revenues; governed by the Congress and/or the President; impose significant risks and rewards on the taxpayer; and/or provide goods and services to the public on a non-market basis[20] should be consolidated in GPFFR. Such entities are referred to hereafter as "consolidation entities."

36. Entities listed in the budget, except for non-federal organizations receiving federal assistance (see par 19), are presumed to qualify as consolidation entities while greater judgment will be needed to classify other organizations.

37. Accountability for consolidation entities rests with the Congress and/or the President. Their governance structure is vertically integrated, such that the chain of command and manner of decision making leads directly to elected officials. Vertical integration may include the establishment of organizational authorities, development and approval of budgets, and the appointment of organizational leaders by the Congress and/or the President.

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Disclosure Entities

38. The federal government may have relationships with organizations afforded a greater degree of autonomy than consolidated entities. Some entities, may exercise powers that are reserved to the federal government as sovereign.

[20] Goods and services are provided on a non-market basis when they are provided free of charge or at charges that bear little relationship to the cost of goods or services.

Other disclosure entities may not themselves carry out missions of the federal government but, instead, are owned or controlled by the federal government as a result of regulatory actions, such as entities in **receivership.** To avoid obscuring information about these more autonomous organizations while still being accountable, such entities are to be disclosed rather than consolidated in GPFFRs. Hereafter, these organizations are referred to as "disclosure entities."

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39. Disclosure entities may maintain a separate legal identity, have a governance structure that vests most decision making authorities in a governing body to insulate the organization from political influence, and/or have relative financial independence.

40. Disclosure entities receive limited or no taxpayer support. Accountability rests with the Congress and/or the President, but they have less direct involvement in decision making than in consolidation entities. Limited risks and rewards fall to the taxpayers. Disclosure entities may provide the same or similar goods and services that consolidation entities do, but are more likely to provide them on a market basis.[22]

41. Disclosure entities may include but are not limited to: quasi governmental and/or financially independent entities, entities in receiverships and **conservatorships**, and entities owned or controlled through federal government intervention actions. In some cases, the relationship with the federal government is not expected to be permanent. The following disclosure entity types are presented to assist in identifying entities that are disclosure entities. The accompanying Appendix C—Illustrations offers non-authoritative hypothetical examples that may be useful in understanding the application of the standards.

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Quasi Governmental and/or Financially Independent Entities

42. Quasi Governmental and/or Financially Independent Entities differ from consolidation entities with regard to governance and/or financial arrangements. Such disclosure entities are on a continuum that considers such factors as whether the governance is through appointed officials versus a structure that vests most decision-making authorities in a governing body to insulate the organization from political influence; whether the entity is financed primarily through taxes and other non-exchange revenues versus limited or no taxpayer support; and whether it provides goods and services on a non-market basis versus provide goods and services on a market basis.

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[22] Goods and services are provided on a market basis when prices are based on the prices charged in a competitive marketplace between willing buyers and sellers.

43. Governance differences typically lead to greater independence. Characteristics may include the following:

    a. Longer appointments of key executives or governing boards to allow these appointees a degree of independence from the Congress and/or the President

    b. Delegated operational authority to provide a service or execute a program in a manner similar to private business enterprises

    c. Private sector legal characteristics, such as not-for-profit status under the Internal Revenue Code

    d. Exemption by statute from laws or regulations dealing with the federal budget, funds, personnel, ethics, acquisition, property, or works

    e. Voluntary association with the federal government and shared purposes to implement government policies

44. Financial differences typically lead to greater fiscal autonomy. Characteristics may include the following:

    a. Primarily funded from a source other than appropriations

    b. Delegated financial authority to provide a service or execute a program in a manner similar to private business enterprises

    c. Principally engaged in selling goods and/or services to organizations outside of the federal government

    d. Intended to, in the normal course of its operations, maintain its operations and meet its liabilities from revenues received from sources outside of the federal government

45. While not all entities of a given type will meet the characteristics above, examples of the types of entities that may be quasi governmental and/or financially independent entities include certain **Federally Funded Research and Development Centers**, museums, performing arts organizations, universities, and venture capital funds. Each individual entity should be assessed objectively since there are likely to be differences among the entities within these example types such that some should be consolidation entities and others disclosure entities.

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Receiverships and Conservatorships[23]

46. The federal government may take control or ownership of failed financial institutions, such as banks, with no goal to maintain control or ownership. Receiverships or conservatorships are established to liquidate failing financial institutions or to guide such institutions back to safe and sound conditions.[24] Entities controlled or owned through receiverships or conservatorships are likely to be disclosure entities.

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Federal Government Intervention Actions Resulting in Control or Ownership

47. The federal government may intervene in exceptional circumstances, such as an economic crisis or military occupation, due to its broad responsibility for the well being of the country. Although intervention actions are not expected to be permanent, they may not include a specific time limit.

48. Typically federal government intervention actions are not routine activities. Strategic planning documents are unlikely to include objectives to routinely initiate such interventions or to permanently operate organizations acquired through interventions.

49. Examples of intervention actions resulting in control or ownership include:

    a. Temporary control with risk of loss or expectation of benefit -- the federal government seizes control of an established organization but expects to relinquish or cede control.

    b. Temporary ownership--the federal government acquires an ownership interest of an organization but expects to end its interest as soon as practicable.

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50. Intervention actions that exist at fiscal year-end must be assessed to confirm the resulting control or ownership is not expected to be permanent. If the intervention activities are not expected to be permanent or other characteristics of disclosure entities exist, organizations controlled or owned as a result of intervention actions would be disclosure entities.

[23] This type differs slightly from federal interventions. Receivership and conservatorship activities are considered part of the mission of the federal reporting entities that perform them and the duration of the relationship is typically shorter.

[24] For example, the Federal Deposit Insurance Corporation (FDIC) is an independent agency created by the Congress with the mission "to maintain stability and public confidence in the nation's financial system by: insuring deposits; examining and supervising financial institutions for safety and soundness and consumer protection; and, managing receiverships."

Component Reporting Entities

51. The government-wide reporting entity is the only federal reporting entity that is an independent economic entity[25] and the inclusion principles are expressed from the perspective of the federal government. However, GPFFRs for the government-wide reporting entity represent a consolidation of component reporting entity GPFFRs. Therefore, component reporting entities must identify and include in their GPFFRs all consolidation and disclosure entities for which they are accountable so that both the component reporting entity and government-wide GPFFRs are complete.

52. A component reporting entity's GPFFR should include all organizations that would allow the Congress and the President to hold its management (appointed officials or other agency heads) accountable for implementation of public policy decisions. Inclusion would also reveal the risks inherent in component reporting entity operations, and enhance accountability to the public. Each component reporting entity is accountable for all consolidation and disclosure entities administratively assigned to it.

53. Administrative assignments to component reporting entities are typically made in policy documents such as laws, budget documents, regulations, or strategic plans. Administrative assignments can be identified by evaluating one or more of the following areas:[26]

    a. Scope of the Budget Process

    b. Accountability Established Within a Component Entity

    c. Misleading to Exclude and/or Misleading to Include

Scope of the Budget Process

[25] SFFAC 2, par. 38.
[26] Component reporting entities should develop processes to ensure organizations in each of the areas identified in par. 53 a.- c. have been considered and assessed. Central agencies are anticipated to determine if there is a need for coordinated guidance to be developed to ensure government-wide consistency.

54. Consolidation and disclosure entities subject to the budget approval and oversight process of the component reporting entity head should be included in the component reporting entity GPFFR. Each component reporting entity should include:

   a. all consolidation entities listed within its section of the *Budget of the United States Government: Analytical Perspectives- Supplemental Materials* schedule *Federal Programs by Agency and Account* unless they are non-federal organizations receiving federal financial assistance[27] and

   b. all disclosure entities included within its Congressional Budget Justification.[28]

Accountability Established Within a Component Reporting Entity

55. Consolidation and disclosure entities for which a component reporting entity has been assigned accountability responsibilities should be included in its GPFFR. Determining whether accountability was established or assigned to a component reporting entity requires the consideration of certain indicators and the application of professional judgment. Indicators[29] that accountability has been established in the component reporting entity include:

   a. Statutes or regulations establishing an organization state that it is assigned to or part of a larger federal organization.[30]

   b. An organization is included in the component reporting entity's published organization chart.

   c. The component reporting entity acquires and/or monitors[31] ownership interests in organizations where there are ongoing responsibilities[32] such as:

      (1) coordinating and/or conveying input on strategic plans,

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<#>monitoring the value of the ownership interest,¶

[27] See par. 19.
[28] The Congressional Budget Justification is the document submitted annually to Congress to justify an organizations budget request.
[29] These indicators provide evidence that accountability was established or was assigned to a component reporting entity. Meeting any one would typically mean accountability was established.
[30] For example, the United States Census Bureau (officially the Bureau of the Census, as defined in Title 13 U.S.C. § 11) is part of the US Department of Commerce.
[31] Such responsibilities may be assigned to a program office.
[32] These responsibilities are examples of actions or activities performed by the component reporting entity indicative of monitoring an ownership interest in an organization, which is an indicator of accountability.

(2) providing appropriated funds to the organization and receiving requests for funding in the current and/or future years, or

(3) administering any federal grants or contracts awarded to the organization.

(4) monitoring activities and/or reporting on outcomes,

(5) monitoring the value of the ownership interest,

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d. A controlled organization[33] was established by statute or by action of the component reporting entity to support the mission of the component reporting entity, and a continuing relationship exists. Examples of continuing relationships include:

(1) approving bylaws including any amendments,

(2) being represented on the governing board (e.g., as an ex-officio member),

(3) appointing members of the governing board,

(4) coordinating and/or conveying input on strategic plans,

(5) monitoring organizational performance,

(6) approving budgets, operating plans, or contracts with others,

(7) establishing and executing cooperative agreements with the organization,

(8) administering federal grants to or contracts with the organization,

(9) testifying before Congress regarding entity performance and objectives, or

(10) significant financial transactions or balances that indicate ongoing managerial involvement.

56. If more than one component reporting entity is assigned responsibilities as described above, the following guidance applies:

[33] Where control exists at the government-wide level based on paragraphs 22-31.

a. Disclosure entities should be included in the GPFFR of each component reporting entity assigned such responsibilities.

b. Consolidation entities should be administratively assigned to only one component reporting entity.[34] The component reporting entity assigned the largest share[35] of responsibilities described in paragraph 55 generally should include the consolidation entity.

57. If a disclosure entity has not been administratively assigned to a consolidation entity, the disclosure entity should be reported by a component reporting entity (a) assigned responsibility for transferring funds to the disclosure entity or (b) with which its mission most closely aligns.

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Misleading to Exclude and / or Misleading to Include

58. There may be instances where an organization is not administratively assigned to the component reporting entity based on the principles in paragraphs 54-57 yet the component reporting entity GPFFR would be misleading or incomplete if the organization were excluded. If so, such organizations should be included in the component reporting entity's GPFFR.[36]

59. There may be instances where applying the principles in paragraphs 54-57 to consolidation entities, would result in misleading presentation for the component reporting entity. For example, an organization may have been legally established within a larger entity while being authorized to operate independently. While such conditions are expected to be rare, if it would be misleading to consolidate the organization in the component reporting entity GPFFR, the organization may be excluded so long as it is consolidated in the government-wide reporting entity.

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60. Determining whether it would be misleading to include a consolidation entity administratively assigned to a component reporting entity requires the application of professional judgment. Examples[37] of indicators that it may be misleading to include an organization are:

[34] Note that the component reporting entity to which a consolidation entity is administratively assigned may also be administratively assigned to a higher level component reporting entity.
[35] Largest share as used here may be assessed based on volume of financial transactions or most significant administrative roles.
[36] Although such situations would be rare, this Statement provides for situations that may arise.
[37] The indicators listed in 60 a. – f. are examples and there may be other indicators not included on this list. Further, no specific number of indicators need be present to determine an organization would be

a. The budget submission is combined for procedural purposes only, as indicated by:

(1) the budget request not being approved by component reporting entity management, or

(2) the absence of involvement by component reporting entity management regarding budget execution, investments, or strategic planning.

b. The component reporting entity provides no direct oversight of the organization.

c. The organization's funding is separate from the component reporting entity's funding.

d. Inclusion of the organization's financial information in the component reporting entity's financial statement could be misleading as to the entity's responsibilities for the organization's liabilities and other obligations.

e. The organization has established itself as a stand-alone organization since its inception and has routinely prepared audited financial statements since that time.

f. The organization provides financial data directly to the Department of the Treasury for the government-wide GPFFR.

GPFFR Consolidation and Disclosure

Consolidation entities

61. Consolidation entities' financial statements should be consolidated to facilitate an assessment of the financial position of the federal government and the cost of operations financed by taxpayers. A component reporting entity should provide consolidated financial statements for all consolidation entities administratively assigned to it. Consolidation[38] aggregates the individual financial amounts of

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misleading to include. This determination is based on the assessment as a whole after considering all facts and often requires professional judgment in making such decisions.

[38] Consolidation is a method of accounting that combines the accounts of those entities line by line on a uniform basis of accounting and eliminates balances and transactions among the entities. For selected

entities comprising a reporting entity and results in presentation of information for a single economic entity representing taxpayer supported activities, resources, and obligations where accountability rests with the Congress and/or the President.

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62. Consolidation entities as defined herein are considered federal entities and should apply GAAP as defined in SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.

63. SFFAS 34 recognizes that a limited number of federal entities prepare and publish financial reports pursuant to the accounting and reporting standards issued by the Financial Accounting Standards Board (FASB). SFFAS 34 provides that GPFFRs prepared in conformity with accounting standards issued by the FASB also may be regarded as in conformity with GAAP. Consolidation entities (i.e. the consolidated government-wide entity or a consolidated component reporting entity) should consolidate component reporting entity or sub-component financial statements for consolidation entities prepared in accordance with SFFAS 34 without conversion for any differences in accounting policies among the entities. Nonetheless, any component reporting entity that publishes financial reports pursuant to the accounting and reporting standards issued by the FASB should disclose intragovernmental amounts measured in accordance with federal financial accounting standards to facilitate elimination entries in preparation of the government-wide financial statements.

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Disclosure entities

64. Maintaining a distinction between the finances of consolidation entities and disclosure entities will more effectively meet federal financial reporting objectives. However, federal financial reporting objectives cannot be fully met without information regarding disclosure entities.

65. For those organizations classified as disclosure entities, this Statement provides for judgment by the preparer in determining the appropriate disclosures based on the factors and principles provided herein. Information regarding disclosure entities should be disclosed in accordance with ***Disclosure Requirements*** as detailed in par. 67 to 70 below after considering the factors listed in par. 66.

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financial statements such as the statement of budgetary resources, a combined financial statement which does not eliminate balances and transactions among the entities is acceptable.

Factors in Determining Disclosures

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66. Materiality is an overarching consideration in financial reporting. Preparers should consider both qualitative and quantitative materiality in determining disclosure entity disclosures. Beyond materiality, the following factors[39] should be considered in making judgments about the extent of appropriate disclosure entity disclosures:

a. ***Relevance to reporting objectives*** - Significance of the disclosure entity to meeting the reporting objectives established in SFFAC 1, *Objectives of Federal Financial Reporting,* with regard to the consolidation entity. In particular, this would include the significance of the information regarding results of operations and financial position to meeting the operating performance and stewardship reporting objectives.

b. ***Nature and magnitude of the potential risks/exposures or benefits associated with the relationship***- Information is needed to provide an understanding of the potential operational or financial impact, including financial-related exposures to potential gain and risk of loss, to the consolidation entity resulting from the disclosure entity's operations.

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c. ***Disclosure entity views/perspective***- (Entities determined to be disclosed in accordance with paragraphs 38 -- 41.) Information about how the disclosure entities account for or report on their relationship with the federal government. For example, whether the disclosure entity views itself as an extension of the federal government or operationally independent of the Congress and/or the President may influence the type and extent of information that is disclosed.

d. ***Complexity of the relationship***- More complex relationships would involve additional detailed disclosures to ensure the relationship is understood by the readers.

e. ***Extent to which the information interests, or may be expected to interest, a wide audience*** - Due to the sensitivity of the relationship,

[39] The factors are presented in a list for consideration in the aggregate; no individual weights should be assigned or interpreted.

materiality of the transactions, media attention, or other reasons, interested parties may expect more extensive information regarding the disclosure entity or its relationship with the federal government.

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f. ***Extent to which there are no alternative sources of reliable information***- An objective of GPFFRs is to meet the needs of users who may have limited access to information or statements and lack the ability to demand the desired information.

Disclosure Requirements

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67. In addition to the factors presented in par. 66 regarding the extent of disclosures, both qualitative and quantitative factors should be considered in determining whether information regarding a disclosure entity should be presented separately due to its significance or aggregated with the information regarding other disclosure entities. If information is aggregated, aggregation may be based on disclosure entity type, class, investment type, or a particular event deemed significant to the reporting entity.

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68. Disclosures should be integrated so that concise, meaningful and transparent information is provided. Integration is accomplished by providing a single comprehensive note regarding the disclosure entity and related balances or by incorporating references to relevant notes elsewhere in the GPFFR but relating to the disclosure entity. For example, a reference may be made to a note regarding investments in the disclosure entity.

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69. For each significant disclosure entity and aggregation of disclosure entities, information should be disclosed to meet the following objectives[40]:

a. ***Relationship and Organization:*** The nature of the federal government's relationship with the disclosure entity or entities

b. ***Relevant Activity:*** Nature and magnitude of relevant activity during the period and balances at the end of the period

c. ***Future exposures:*** A description of financial and non-financial risks and potential benefits and, if possible, the amount of the federal government's exposure to gains and losses from the past or future operations of the disclosure entity

[40] The objectives are not listed in any order of preference.

70. Examples of information that may meet the above objectives and provide the necessary understanding of the disclosure entity's relationship and organization, activities, and future exposures specific to the federal government are provided below.[41] In determining what information is needed to meet the objectives in paragraph 69, the factors in paragraph 66, including the complexity and nature and magnitude of the relationship, should be considered. The list of examples below may not be exhaustive and additional items of information necessary to meet the objectives should be disclosed even if not specifically identified in the list below.

a. The name and description of the disclosure entity,[42] including information about how its mission relates to federal policy objectives, organization and any significant involvements with outside parties

b. The nature of the relationship between the federal government and the disclosure entity including relevant information regarding:

(1) How any control or influence over the disclosure entity is exercised

(2) Key terms of contractual agreements, statutes, or other legal authorities

(3) The percentage of ownership interest and/or voting rights

c. For intervention actions the primary reasons for the intervention and a brief description of the federal government's plan relative to monitoring, operating and/or disposing of the disclosure entity and/or a statement that the intervention is not expected to be permanent

d. A description and summary of assets, liabilities, revenues, expenses, gains, and losses recognized in the financial statements of the reporting entity as a consequence of transactions with or interests in the disclosure entity and the basis for determining the amounts reported (or a reference to other disclosures where such information is provided)

e. A discussion of key financial indicators and changes in key financial indicators

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[41] No individual example is itself a required disclosure nor are the examples required in the aggregate. Therefore, the examples are not alternatives or substitutes one for another. Rather, a disclosure that meets the objectives in paragraph 69 should be provided.

[42] For simplicity, information is described in relation to a single disclosure entity. Nonetheless, the information may be presented for an aggregation of similar disclosure entities.

f. Information regarding the availability of the disclosure entity's annual financial report and how it can be obtained

g. In the event that contractual agreements, statues, or other legal authorities obligate the consolidation entity to provide financial support to the disclosure entity in the future, information regarding potential financial impacts (including those terms of the arrangements to provide financial support and liquidity, including events or circumstances that could expose the federal government to a loss)

h. The nature of, and changes in, the risks and benefits associated with the control of, or other involvement with, the entity during the period

i. The amount that best represents the federal government's maximum exposure to gain or loss from its involvement with the disclosure entity, including how the maximum exposure to gain or loss is determined. If this cannot be quantified, a narrative discussion could be offered.

j. Other information that would provide an understanding of the potential financial impact, including financial-related exposures to potential gain and risk of loss to the reporting entity, resulting from the disclosure entity's operations including important existing, currently-known demands, risks, uncertainties, events, conditions and trends—both favorable and unfavorable.

71. Disclosure entity information presented in the GPFFR should be based on accrual basis standards provided in generally accepted accounting principles or an other comprehensive basis of accounting developed for its specific type of entity.[44] This includes generally accepted accounting principles for the relevant domain (FASAB, Governmental Accounting Standards Board, or FASB).

72. When information is derived from the disclosure entity's financial report, it is preferable but not mandatory that the report be for the same reporting period as the government-wide reporting entity. If a disclosure entity's reporting period differs from the government-wide reporting entity's and it is not cost-beneficial to align the reporting periods, any financial information disclosed from the disclosure entity's financial report should be for a reporting period ending within the government-wide reporting entity's reporting period.

[44] Consolidation entities should apply the GAAP hierarchy established in SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.

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<#>If the non-core entity exercises powers reserved to the federal government as sovereign, disclosures[43] about such entities should include, at a minimum, information regarding:¶
<#>Its mission¶
<#>The relationship of its mission to federal policy objectives¶
<#>Its organizational structure¶
<#>Nature and magnitude of relevant activity during the period and balances at the end of the period¶
<#>A description of financial and non-financial risks and potential benefits¶
<#>If possible, the amount of the federal government's exposure to gains and losses from the past or future operations¶
<#>The availability of its annual financial report and how it can be obtained ¶

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73. Significant changes in information occurring from the end of the disclosure entity's reporting period should be reported consistent with the requirements of SFFAS 39, *Subsequent Events: Codification of Accounting and Financial Reporting Standards Contained in the AICPA Statements on Auditing Standards*.

Related Party

74. In addition to entities for which Congress and the President are accountable[45], the federal government may have the ability to exercise significant influence over other organizations in making financial and operating decisions or to be influenced by its relationship with the other organizations. Such relationships are numerous and not all warrant disclosure. Guidance is provided below but judgment will also be required to identify relationships that warrant disclosure as related parties.

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75. **Related parties** are not controlled or owned by the federal government. Organizations are considered to be related parties if the existing relationship[46] or one party to the existing relationship has the ability to exercise significant influence over the other party in making financial and operating decisions.

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76. Significant influence (for the purpose of this Statement) is the power to participate in the financial and operating policy decisions of an entity, but not control those policies. Significant influence may be exercised in several ways, sometimes by representation on the board of directors or equivalent governing body but also by, for example, participation in the policy making process, interchange of managerial personnel, or dependence on technical information. Significant influence may be gained by an ownership interest, statute, or agreement.

77. Significant influence does not arise from regulatory actions or economic dependency alone. However, regulation or economic dependency, together with other factors, may give rise to significant influence and therefore a related party relationship. Judgment is required in assessing the impact of regulation and economic dependence on a relationship.

[45] Entities for which the Congress and President are accountable are in the budget, owned, or controlled and would meet the inclusion principles and be reported as either a consolidation or disclosure entity and not be subject to related party reporting.

[46] Relationship as used in this context refers to material transactions or events involving both parties.

78. Although significant influence exists among the component reporting entities of the federal government, component reporting entities are subject to the overall direction and operate together to achieve the policies of the federal government and are not considered related parties. Therefore, component reporting entities need not be disclosed as related parties by other component reporting entities.

79. Further, in the context of this Statement, related parties are organizations with the ability to exercise significant influence –financially and operationally – such that it would be misleading to exclude disclosures regarding the relationship. Related parties *generally* would include but are not limited to:

   a. Government sponsored enterprises not meeting the Inclusion Principles

   b. Organizations governed by representatives from each of the governments that created the organization, including the United States, wherein the federal government has agreed to ongoing or contingent financial support to accomplish shared objectives (for example, multi-lateral development banks)

80. In the context of this Statement, the following *generally* would not be considered related parties:

   a. Entities meeting the Inclusion Principles

   b. Organizations with which the federal government transacts a significant volume of business resulting in economic dependence such as government contractors, state and local governments, collegial institutions and non-profit organizations

   c. Key executives

   d. Organizations owned or managed by key executives, other employees, or members of their families

   e. Component reporting entities of the federal government (see full discussion in par. 78)

   f. Foreign governments

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g. Organizations created through treaties or trade agreements that define common goals and means for joint action where the U.S. role in governing and financing the organizations is not significant

h. Special interest groups[47]

81. Although par. 80 *generally* permits the exclusion of certain organziations as related parties, other factors may create a need for related party reporting and disclosures. The use of judgment will be necessary in identifying those factors consistent with the information needs described in par 82.

82. Certain information regarding related party relationships may enable users to better understand the financial statements of the reporting entity because:

a. Related party relationships might expose the federal government to risks or provide opportunities that would not have existed in the absence of the relationship;

b. Related party relationships can influence the way in which the federal government operates with other entities in achieving its individual objectives; and

c. Related parties may enter into transactions that unrelated parties would not enter into, or may agree to transactions on different terms and conditions than those that would normally be available to unrelated parties.

83. For any Related Party, the following should be disclosed:

a. Nature of the federal government's relationship with the entity, including the name of the entity or if aggregated, a description of the related parties. Such information also would include as appropriate: the percentage of ownership interest.

b. Other information that would provide an understanding of the relationship and potential financial reporting impact, including financial-related exposures to potential gain and risk of loss to the reporting entity resulting from the relationship.

[47] Special Interest groups refers broadly to organizations whose members share common concerns and try to influence government policies. Examples include but are not limited to International Brotherhood of Teamsters, American Public Power Association, Christian Coalition, the National Organization for Women (NOW) and the National Rifle Association (NRA)

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Effect on Existing Concepts-- Proposed Amendments to SFFAC 2, *Entity and Display*

84. The purpose of this section of the Statement is to propose amendments to Statement of Federal Financial Accounting Concepts (SFFAC) 2, *Entity and Display,* as described in the following paragraphs.

85. Conforming changes have been proposed to SFFAC 2. Paragraphs 54—77 and 79 – 112 address concepts outside the scope of this Statement and are not amended.

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86. Paragraph 2 is replaced with the following paragraph which describes the amended purpose and contents of the Statement.

> The purpose of this statement is to establish concepts regarding what would be encompassed by a Federal Government entity's financial report. The statement specifies the types of entities for which there should be financial reports (hereinafter called reporting entities), establishes an organizational perspective for considering the makeup of each type of reporting entity, identifies types of financial reports for communicating the information for each type of reporting entity, suggests the types of information each type of report would convey, and identifies the process and factors the Board may consider in determining whether information should be basic information, required supplementary information (RSI), or other accompanying information (OAI).

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87. Paragraphs 3 - 5 are rescinded because the preamble applicable to all concepts statements, which was adopted at the time SFFAC 5 was issued, addresses the topics covered.

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88. Paragraph 6a below is inserted following paragraph 6 to recognize the importance of accountability in determining organizations to be included in the reporting entity GPFFR:

> 6a. SFFAC 1 also discusses accountability and users' information needs as the foundation for the objectives of federal financial reporting.

Specifically, par. 71 states "It may be said that 'accountability' and its corollary, 'decision usefulness,' comprise the two fundamental values of governmental accounting and financial reporting. They provide the foundation for the objectives of federal financial reporting. …The assertion of accountability therefore leads to identifying, first, those to whom government is accountable and, second, the information needed to maintain and demonstrate that accountability." Based on the concepts established in SFFAC 1, it is clear accountability is a fundamental goal of financial reporting to be considered in establishing the boundaries of general purpose federal financial reports.

89. Paragraph 7 is rescinded because it is covered by the new preamble to statements of federal financial accounting concepts.

90. Paragraph 10, first bulleted item is amended by replacing it with the following bulleted item addressing an understanding of what the reporting entity entails:

- ensure information at each reporting level includes information about all relevant organizations to support accountability by including organizations that are in the budget, owned, or controlled with risk of loss or expectation of benefit;

91. Paragraph 38 is amended to exclude references to other paragraphs amended by this Statement. Paragraph 38 is replaced with the following:

> The ultimate aggregation of organizations is into the Federal Government which, in reality, is the only independent economic entity. The Federal Government encompasses all of the resources and responsibilities existing within the component reporting entities. The aggregation would include organizations for which the Federal Government is financially accountable as well as other organizations for which the nature and significance of their relationship with the government are such that their exclusion would cause the Federal Government's financial statements to be misleading or incomplete.

92. Paragraphs 39 -50 are rescinded because they go beyond conceptual guidance and appear to establish standards within a concepts statement. Deleting these paragraphs will avoid any confusion regarding the role of the inclusion principles presented in the draft standards without creating a void in concepts.

93. The sub heading before paragraph 51 - "Other Aspects Concerning Completeness of the Entity" - is revised to read "Other Aspects Concerning Completeness of the Component Reporting Entity."

Comment [ML2]: Paragraph 8 will remain in SFFAC 2. Board member comment that it does not relate to entity. However, staff believed it appeared to go beyond a concept but will maintain as it appears to go beyond the scope of this project.

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ensure that organizations are not included in the reporting entity if the federal government does not own them or have the ability to control them or if they are not included in the budget

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94. Paragraph 51 is replaced with the following:

> Identifying the organizations to include in the reporting entity is one aspect of ensuring that the users of a reporting entity's financial reports are provided with all the information relevant to the reporting entity. However, because the only independent economic entity is the entire Federal Government, financial resources or free services are often provided from one component in the government to another component without a quid pro quo. For example, a portion of the retirement costs of Federal employees is reported by the Office of Personnel Management rather than the organizational entities employing the persons. Thus, within parameters more appropriately established in accounting standards, it is important to ensure that the reporting entity's financial reports include amounts that are attributable to the reporting entity's activities, even though they are recorded elsewhere. This is particularly important for costs associated with the use of human resources; personnel services are such a major part of most government activities. It is also important for the costs of services provided by other reporting entities, such as computer services provided by another unit.

95. Paragraphs 52 – 53 are rescinded because these paragraphs relate to issues covered in standards and are not necessary for understanding the notion of the reporting entity.

96. A new sub-heading "Need to Distinguish between Consolidation and Disclosure Entities" is inserted at paragraph 53A.

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97. Insert Paragraphs 53A – 53 E. under the sub-heading: "Need to Distinguish between Consolidation and Disclosure Entities" - The proposed language provides a high level explanation of consolidation and disclosure entities. These are new terms introduced in the proposed Statement and critical to understanding the reporting entity concept in the federal government. More importantly, the proposed language describes the need to distinguish them and the reason for this distinction in terms of financial statement presentation.

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> 53A. The Federal Government is a large and complex organization. In order to fulfill public policy objectives, the federal government may rely both on consolidation entities (such as departments and agencies) and on organizations that are distinct from consolidation entities to fulfill public policy objectives (such as financially independent organizations). These distinct entities are referred to collectively as disclosure entities.

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> 53B. Disclosure entities may maintain a separate legal identity, have a governance structure designed to insulate the organization from political influence, and/or be granted relative financial independence. Despite disclosure entities' relative operational and financial independence, accountability for all organizations owned or controlled by the Federal Government rests with the

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Congress and/or the President. So, both consolidation and disclosure entities should be included in financial reports to provide accountability.

53C. It may be difficult to provide accountability, by meeting financial reporting objectives, through consolidated financial statements because they blur the distinction between consolidation entities and disclosure entities. Consolidated financial statements may obscure the fact that resources and resource allocation decisions for disclosure entities are more independent. While consolidation entities are financed by taxpayers and governed directly by elected officials, disclosure entities often do not rely on taxpayers for financing or elected officials for spending authority. For example, a single-column presentation of information for all entities likely would create a risk of incorrect inferences. Such inferences may include the amount of assets and revenues available for consolidation entities to use in general government activities, and the extent to which taxpayers stand ready to liquidate liabilities and meet expenses of disclosure entities.

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53D. Maintaining a distinction between consolidation entities and disclosure entities may more effectively meet federal financial reporting objectives. Such a distinction may be maintained through discrete presentation of information regarding disclosure entities. For example, disclosure by the government, including component reporting entities, of information regarding disclosure entities may provide needed information about disclosure entities. Nonetheless, disclosures are not a substitute for consolidation entities recognizing the financial effects of transactions with disclosure entities.

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53E. Consolidated financial statements for only consolidation entities will facilitate an assessment of the financial position of the federal government and the cost of operations financed by taxpayers. Consolidation aggregates the individual financial statements of entities comprising a reporting entity and results in presentation of information for a single economic entity representing consolidated taxpayer supported activities, resources, and obligations. Consolidation entities are considered federal entities and should apply GAAP as defined in SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board.* The following sections discuss display of information in consolidation entity financial reports.

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98. Paragraph 78 is rescinded because it is not conceptual guidance. It identifies an expectation that material differences between the recognition and measurement requirements under the Financial Accounting Standards Board and the FASAB standards will be adjusted before consolidation. This issue is to be addressed in standards.

Effective Date

99. This Statement is effective for periods beginning after September 30, 2015. Earlier implementation is encouraged.

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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.

Introduction

A1. The federal government and its relationships with other organizations have become increasingly complex. These complex relationships make it difficult to identify federal entities. In addition, some organizations may be viewed as “non-federal” and yet be owned or controlled by the federal government. Identifying the organizations to be included in the government-wide and component reporting entity general purpose federal financial reports (GPFFR) is necessary to ensure their completeness.

A2. The GPFFR should include the varied organizations for which the Congress and/or the President are accountable regardless of their form. Therefore, the primary reason for developing standards for the government-wide and component reporting entity GPFFRs is to ensure that users will be provided with complete financial information about the federal government and its involvements. While SFFAC 2, *Entity and Display*, provides criteria for determining if an organization should be included, questions have continued in this area that resulted in the need for standards.

Project History /Task Force

A3. In 2008, the Board formed a task force to support the project. The objective of the task force was “to assist in developing the proposed standards on the boundaries of the reporting entity and specific criteria for determining whether an organization should be included.”

A4. The task force met several times over the course of the project and also exchanged numerous ideas and recommendations electronically. The task force views and recommendations were presented to the Board for their consideration during the development of these proposed standards. Their assistance was essential and their views carefully considered by members during deliberations. (See Appendix F for a list of task force members.)

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Organizational Approach to Defining Boundaries

Underlying Concepts

A5. The federal government is complex and therefore defining the boundary of GPFFRs may be difficult. Its constitutionally established powers and often its motivations and functions are different from other organizations. Despite these complexities, difficulties, and differences, accountability is a fundamental goal of financial reporting. As noted in SFFAC 1:

> The federal government derives its just powers from the consent of the governed. It therefore has a special responsibility to report on its actions and the results of those actions. These reports must accurately reflect the distinctive nature of the federal government and must provide information useful to the citizens, their elected representatives, federal executives, and program managers. Providing this information to the public, the news media, and elected officials is an essential part of accountability in government.[48]

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A6. SFFAC 1 discusses accountability and users' information needs as the foundation of governmental financial reporting. Specifically, par. 71 states "It may be said that 'accountability' and its corollary, 'decision usefulness,' comprise the two fundamental values of governmental accounting and financial reporting. They provide the foundation for the objectives of federal financial reporting. …The assertion of accountability therefore leads to identifying, first, those to whom government is accountable and, second, the information needed to maintain and demonstrate that accountability."

A7. SFFAC 1 explains that the federal government has a special responsibility to report on its actions and the results of those actions. SFFAC 1 discusses the information needs of both internal and external users including the citizens, their elected representatives, federal executives, and program managers because meeting user information needs is an essential part of accountability in government.

A8. An organizationally based approach to defining boundaries supports accountability to all users but particularly to external users who may be unaware of the nature of organizational relationships. Focusing on organizations helps to identify who is accountable and for what. In addition, an

[48] SFFAC 1, paragraph 8.

organizational approach provides meaningful financial statements by aligning boundaries with defined organizations for which there would likely be users of GPFFRs.[49]

Identifying and Classifying Organizations

A9. This Statement provides that reporting entities should first identify what organizations are to be included[50] in the reports. The three principles for including organizations in the government-wide GPFFR are: *In the Budget*, *Majority Ownership Interest*, and *Control with Risk of Loss or Expectation of Benefit*. The Statement also includes a provision requiring inclusion of an organization if it would be misleading to exclude it.

A10. Next, for those organizations to be included, a distinction is made between consolidation entities and disclosure entities. This distinction determines how financial information is to be presented in the GPFFR. Consolidation entity financial information is to be provided in consolidated financial statements and related notes. Disclosure entity financial information is to be disclosed in notes to the financial statements.

A11. Professional judgment is required in the application of the standards proposed in this Statement. This Statement presents a principles-based approach to determining which organizations should be included[51] in the government-wide GPFFR because of the wide and varying relationships of the federal government. General purpose federal financial reports for the government-wide reporting entity should be broad enough to report the Congress and the President's accountability for organizations, as well as the Judicial Branch. This ensures that the financial reports contain all the information essential for fair presentation of the government's financial position and results of operations.

A12. The Board considered several alternative approaches to identifying organizations for which elected officials – the Congress and/or the President – are accountable. The principles for inclusion proposed herein establish accountability for organizations (1) funded through the budgetary process, (2) where a majority ownership interest is held, or (3) controlled with risk of loss or

[49] See SFFAC 2, paragraphs 29-38, for a discussion of the organizational approach.

[50] 'Included' means an organization's information is either consolidated or disclosed.

[51] Note that this Statement does not specify which organizations must prepare and issue financial statements.

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<#>SFFAC 1 is very clear that the objectives were designed to help ensure the accountability of the federal government and to better inform decisions influenced by financial information about the government. There is a focus on the needs of current and potential users of federal financial information. In each of the four federal financial reporting objectives articulated in SFFAC 1 there are several references to user information needs and accountability. Clearly, the notion of accountability is important when considering the boundaries of GPFFR.¶

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expectation of benefit. Each of these principles for inclusion is discussed below.

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Principles for Inclusion in the Government-wide GPFFR

In the Budget

A13. Identification of an organization in the President's Budget is the clearest evidence that an entity should be included in the government-wide report. Absent budgetary actions – originating with the President's Budget and leading to appropriations – federal organizations would be unable to continue operations. Financial reporting objectives – budgetary integrity, operating performance, stewardship, and systems and controls – could not be met if organizations identified in the budget were not included in the financial reports. Therefore, the most efficient means to identify organizations for inclusion is by their participation in the budget process as evidenced by the *Budget of the United States Government: Analytical Perspectives- Supplemental Materials* schedule *Federal Programs by Agency and Account*.

A14. Although the legislative and judicial branches (and most organizations within those branches) are not currently required to prepare financial statements, based on this principle (*In the Budget)* those organizations would be reported upon in the government-wide report.[52]

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A15. Organizations should include any financing accounts associated with the organization although such accounts may not be specifically identified in the schedule. For example, the *Federal Programs by Agency and Account* may not identify federal credit reform financing accounts, but those accounts should be included in GPFFR for the organization. In addition, other GAAP principles would apply, such as SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* and SFFAS 5, *Accounting for Liabilities of the Federal Government,* and help identify the elements and required disclosures for each organization.

[52] As the source of GAAP for federal reporting entities, FASAB GAAP would be the appropriate accounting standards for these entities to adopt to the extent they prepare GAAP-based financial statements.

Organizations receiving federal financial assistance

A16. The *Federal Programs by Agency and Account* schedule also sometimes names specific recipients of federal financial assistance. SFFAC 2 acknowledges that the *Federal Programs by Agency and Account* schedule sometimes names an organization to receive a “subsidy” and states “This does not mean, however, that an appropriation that finances a subsidy to a non-Federal entity would, by itself, require the recipient to be included in the financial statements of the organization or program that expends the appropriation.” Thus, “subsidy” is the term used in SFFAC 2 to distinguish such “non-federal” organizations from the organizations intended to be included in the GPFFR.

A17. While the provision in SFFAC 2 was correct, the Board is proposing standards, and believes terms used in this Statement should be defined. The Board considered ways to define “subsidy” but concluded it was more appropriate to rely on the existing definition of “federal financial assistance.”

A18. The proposed language ensures organizations that receive assistance as defined by the Single Audit Act Amendments of 1996[53] but listed under an appropriation in the *Federal Programs by Agency and Account* aren’t automatically included in the GPFFR. Often grants are received through programs and recipient organizations are not necessarily listed in the budget, but an organization may be listed in some cases. The Board believes a means to confirm whether specifically identified recipient organizations are “non-federal organizations receiving federal financial assistance” is needed. When such organizations are listed in the budget they should be assessed against the Majority Ownership Interest and Control with Risk of Loss or expectation of Benefit principles before being excluded from the government-wide GPFFR.

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A19. Generally, the Board believes preparers can identify organizations that are in fact receiving ‘subsidies’ as described by SFFAC 2. The Statement provides that although these may be listed in the budget they are neither automatically included based on the first inclusion principle nor automatically excluded based on the assumption or perception that they would not be owned or controlled. The Board does not believe it would be appropriate to articulate how subsidies are presented in the *Federal Programs by Agency and Account* schedule or refer to other budget documents because such treatments may change.

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[53]'Federal financial assistance' is assistance that non-federal entities receive or administer in the form of grants, loans, loan guarantees, property, cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, or other assistance.

Organizations partially in the budget

A20. The Board deliberated the issue of certain organizations being partially in the budget (i.e., some of their operations or accounts are not in the President's Budget), such as a museum receiving substantial donor support. The Board determined the organization should be included in the government-wide GPFFR based on the *in the budget* principle. The Board further decided that such organizations should be presented in the same manner as other consolidation or disclosure entity, as discussed later in the Statement. Therefore, the language in the principle (*in the budget*) does not provide separate and distinct guidance for organizations partially funded by non-budgetary sources. This means the organization – in its entirety - is either a consolidation or a disclosure entity. Further, paragraph 36 provides that entities listed in the budget are presumed to be consolidation entities.

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Need for Additional Principles

A21. While the principle *in the Budget* is the most efficient means to identify organizations for inclusion, there are additional principles to be considered to identify other organizations that should be included in the government-wide GPFFR. The budget principle represents a starting point in analysis but accountability goals could not be met solely through that principle. Because the budget's purposes differ from financial reporting objectives in many respects (such as the focus on the allocation of budgetary resource flows versus costs of operations), it is possible that organizations or activities might be excluded from the budget for reasons that do not justify exclusion from financial reports. For example, some organizations may be established to operate in a manner similar to businesses and excluded from the budgetary process. Therefore, additional inclusion principles are necessary to ensure completeness in the context of the federal financial reporting objectives.

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Majority Ownership Interest

A22. Ownership interests typically provide owners access to resources and exposure to risks while supporting their desired goals. Federal financial reporting objectives require that information about the service efforts, costs, and accomplishments be made available. To ensure such information is included, when the federal government holds a majority ownership in an organization it should be included in the GPFFR. As described in the

Statement, majority ownership interest exists with over 50% of the voting rights or the net residual assets of an organization.

A23. The Board noted that some may wonder how to account for minority ownership interests (less than 50%). The Board agreed addressing minority interests through the project is likely to be less effective than allowing the GAAP hierarchy to fill any void. To address the potential question, the Board included within the Statement a footnote stating ownership interests 50% or less should be accounted for in accordance with the appropriate accounting standards per the GAAP hierarchy.

Control with Risk of Loss or Expectation of Benefit

A24. When the federal government controls an organization with risk of loss or expectation of benefit, the organization should be included in the government-wide GPFFR to provide accountability. As detailed in the Statement, control involves the power to impose will on and/or govern the financial and/or operating policies of another organization with the potential to obtain financial resources or non-financial benefits or be obligated to provide financial support or assume financial obligations as a result of those actions. Both the power and the risk of loss and expectation of benefit aspects of the control definition should be present to justify inclusion of the organization in the GPFFR.

A25. For example, the Statement provides for situations where the risk of loss or expectation of benefit does not exist—in the instance of the federal government exercising regulatory powers over an organization. In these cases, the federal government is unable to exercise that power for its own benefit and rarely explicitly assumes risk of loss. Therefore, including such an organization in the GPFFR would misrepresent the financial position and results of operation of the government. This would not support achievement of the objectives of financial reporting.

A26. For financial reporting purposes, assessment of control is made at the reporting date and based on current legislation, rather than legislation that may or may not be enacted in the future.

A27. Determining control requires judgment, and the Statement provides indicators to assist in making determinations. The first set of indicators is "persuasive" as the federal government has the authority to control and any one of the listed items would mean control is present. The second set of indicators requires more judgment because the set of indicators is considered in the aggregate to assess whether the federal government has the ability to control the organization.

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A28. Because the government does not usually seek only financial benefits, the expected *benefit* associated with control does not have to be a financial benefit. Instead, it may be non-financial. For example, it may be in the form of a service provided on the federal government's behalf or the ability to direct the work of the other entity to deliver goods and services.

Misleading to Exclude Principle

A29. The Statement includes a general provision requiring inclusion of an organization if it would be misleading to exclude it. Certain members believed this may be problematic because no criteria are offered. However the Board ultimately agreed the general provision could accommodate rare situations that may arise in the future. This is consistent with provisions of SFFAC 2.

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A30. The Board also believes the principle is consistent with the Governmental Accounting Standards Board Statement 14, *The Financial Reporting Entity.* It provides for those unique situations where the preparer and auditor agree an organization should be included that was not otherwise incorporated as a result of the principles. Judgment would be required in this area. Therefore, the Board provides for judgment rather than attempting to anticipate these types of situations and develop criteria.

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Reporting on Organizations—Consolidation or Disclosure

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A31. Differences in purposes and governance structures by organizations may require differences in presentation of related financial information. This Statement provides that the reporting entity should first determine which organizations are to be included in the reports. Next the reporting entity should classify the included organizations between consolidation entities and disclosure entities.

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A32. Different means of presenting relevant information are provided for consolidation and disclosure entities. The distinction between consolidation entities and disclosure entities is based on the degree to which the following characteristics are met: the entity is taxpayer supported, is governed by the Congress and/or the President, imposes or may impose risks and rewards on the taxpayer, and/or provides goods and services on a non-market basis. Maintaining a distinction between consolidation entities where accountability rests with the Congress and/or the President, and disclosure entities that are more financially (or operationally) independent will provide information to users that is more understandable and relevant. In some cases, disclosure of information regarding an individual entity is more useful than consolidation of the individual entity's financial statements in the government-wide financial statements. In other cases, consolidation of individual entities' financial statements is needed to provide fair presentation of activities financed by the taxpayers, accountable to the Congress and/or the President, and/or relying on the taxpayers to settle liabilities.

A33. The Board considered whether the proposed principle-based standards were likely to result in fair presentation of certain significant entities or classes of entities. For example, in considering the Federal Reserve System, some members believe that consolidation might obscure the financial effects of fiscal policies while disclosure might shed more light on monetary policy. However, one member believes consolidation of the Federal Reserve System is appropriate and any obscurity that may occur could be made clear through the notes to the financial statements. The Federal Reserve System is presently structured to facilitate monetary policy decisions that are independent of fiscal policy decisions by the President and Congress.

A34. Because monetary policy decisions are often executed through the purchase and sale of Treasury securities in the open market,[54] Treasury securities are a significant asset of the Federal Reserve Banks. If the Federal Reserve System is consolidated in the government-wide financial statements, any Treasury securities held as assets by the Federal Reserve System would be eliminated against the Treasury securities identified as liabilities. Accordingly, this use of Treasury securities to conduct monetary policy may introduce volatility and variability in the reported amount of Treasury securities outstanding unrelated to the fiscal policies of the federal government. Changes in these amounts arising from budgetary deficits and surpluses could be obscured by changes arising from monetary policy. In addition, liabilities for Federal Reserve notes outstanding and deposits by depository institutions would be reported on the consolidated balance sheet. These liabilities differ in character from liabilities arising from fiscal policy and may distort the government-wide financial statements.

A35. In contrast to consolidation, disclosures regarding the Federal Reserve System may aid users in understanding the Federal Reserve System, its relationship with the federal government, and any significant activities or risks posed to taxpayers. Principle-based standards do not result in the Board deliberating on

[54] The Federal Reserve Act, Section 14, authorizes Federal Reserve banks to buy and sell bonds and notes of the United States but requires when they exercise this authority and purchase or sell Treasury Securities, it must be done in the open market (rather than directly from or to the Treasury).

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Deleted: purchases of Treasury Securities in the open market (rather than directly from the Treasury) the classification of the Federal Reserve System or any other specific entity. However, deliberations were conducted to assure the Board that the proposed standards were adequate and the elements of the standards were appropriate for application given the unique role of the central bank.

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Consolidation entities

A36. Consolidation entities generally provide goods and services on a non-market basis. That is, prices are not established solely through market transactions where supply and demand determine price. Goods and services provided on a non-market basis may be free of charge or provided at prices that are either not economically significant or bear little relationship to the cost of the goods or services.

A37. Consolidation entities are financed through taxes, fees and other non-exchange revenue as evidenced by inclusion in the budget. Significant risks and rewards fall to the taxpayer for consolidation entities. Inclusion in the budget is the clearest evidence an entity is relying on the taxpayer and that elected officials are key decision makers.

A38. The budget is a political document serving many purposes. The 1967 *Report of the President's Commission on Budget Concepts* indicates that "the budget must serve simultaneously as an aid in decisions about both the efficient allocation of resources among competing claims and economic stabilization and growth." On the topic of coverage of the budget, the Commission recommended that "the budget should, as a general rule, be comprehensive of the full range of Federal activities." Because the budget includes "federal activities," entities listed in the budget, except those receiving federal financial assistance, are presumed to qualify as consolidation entities. For such entities, allocation of resources to its activities is determined through federal legislation – making the entity itself financially accountable to the Congress and/or the President. Accountability to citizens for consolidation entities ultimately rests with the Congress and/or the President, and their approved appointed organizational leaders.

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A39. The assessment of whether an entity meets the attributes for a consolidation entity is based on the assessment of all the attributes and the degree to which each is met. As such, not all attributes are required to be met; classification is based on the assessment as a whole. For example, the post office may compete against other organizations; therefore it may be viewed as providing goods and services on a market basis. However, if it primarily meets the remaining characteristics then it is a consolidation entity.

Disclosure entities

A40. On the opposite end of the spectrum and with varying degrees in between are disclosure entities. The use of professional judgment will be required when identifying the disclosure entities as there is a broad spectrum of entities having varying degrees of relationships with the federal government.

A41. Disclosure entities receive limited or no taxpayer support. Disclosure entities, in contrast to consolidation entities, are often structured so there is a clear barrier or limit on taxpayer financing of the entity. This is an effort to shield the taxpayer from risk.

A42. In addition, another contrast with consolidation entities is that with disclosure entities, accountability ultimately rests with the Congress and/or the President but there is much less direct involvement in decision making. Greater accountability for decision making may rest with an independent governing board and there may be situations where disclosure entities may have a separate legal identity.

A43. It is important to recognize the continuum that exists among disclosure entities. For example, despite a greater degree of autonomy, some disclosure entities may still exercise powers that are reserved to the federal government as sovereign. Other disclosure entities may not themselves carry out missions of the federal government but, instead, are owned or controlled by the federal government as a result of regulatory or intervention actions.

A44. The Statement provides categories of disclosure entities primarily as a way to help identify disclosure entities. However, the Statement does not require presentation by any specific class or category and allows flexibility in presenting information about disclosure entities. The categories of disclosure entities include quasi governmental and/or financially independent entities, receiverships and conservatorships, and federal government intervention actions.

Quasi Governmental and/or Financially Independent Entities

A45. The Statement describes quasi governmental and/or financially independent entities as those disclosure entities where governance and/or financial differences lead to greater independence. The Statement provides both governance and financial characteristics that would be found in this type of disclosure entity.

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A46. Quasi governmental and/or financially independent entities may include certain Federally Funded Research and Development Centers (FFRDC), museums, performing arts organizations and universities, and venture capital funds. Because details may differ among organizations in each example type, an objective assessment may classify some individual organizations as consolidation entities rather than disclosure entities. The accompanying Illustrative Guide offers examples that may be useful in application.

Receiverships and Conservatorships

A47. The Statement describes receiverships and conservatorships as disclosure entities. This includes those failed financial institutions and banks the federal government takes control or ownership of with no goal to maintain the relationship. Absent a decision to make control permanent, such controlled or owned entities would be disclosure entities.

Federal Government Intervention Actions

A48. The Statement describes federal government intervention actions as disclosure entity involvements resulting from exceptional circumstances where the involvements are not expected to be permanent. SFFAC 1 acknowledges the unique nature of federal government activity and its broad responsibilities. Par. 50 explains "The federal government is unique, when compared with any other entity in the country, because it is the vehicle through which the citizens of the United States exercise their sovereign power. The federal government has the power through law, regulation, and taxation to exercise ultimate control over many facets of the national economy and society…" SFFAC 1 describes the federal government's responsibility for the general welfare of the nation in par. 53-54 as "a broad responsibility that involves multiple goals."

A49. With these broad responsibilities, the federal government may decide to take certain actions or intervene in certain situations. Examples may include actions to provide stability to the financial markets, key industries, states, cities, counties, or military occupation of another country.[55] These types of federal government interventions are considered rare.[56] Historically the federal

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[55] After the signing of the Japanese Instrument of Surrender in 1945, Japan was supervised for 6 years by the Allied (primarily American) forces and subject to military control, with General MacArthur at the head of the Occupation administration. (Takemae, Eiji 2002 p. xxvi and Wikipedia http://en.wikipedia.org.wiki/Occupation_of_Japan)

[56] The financial crisis that began in 2007 is considered to be the most severe since the Great Depression. (White Paper on Changes to Financial Regulations)

government has been involved in few commercial enterprises on an equity basis or shared ownership basis.[57] As a sovereign entity, the federal government does not act to maximize profits. In doing so, the federal government may intervene and act in capacities to protect taxpayers which may ultimately lead to taking control of organizations or acquiring some form of ownership.

A50. The federal government may also intervene by providing assistance through extending loans or debt guarantees that do not meet the inclusion principles established in this Statement. Such transactions should be accounted for in accordance with the appropriate accounting standards per the GAAP hierarchy. This Statement does not include additional disclosures for such intervention actions. Some members believe a single Statement should address all types of intervention actions.

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A51. Currently SFFAC 2 provides an exception for situations where the indicative criteria, leading to consolidation, are met temporarily. Specifically, par. 45 of SFFAC 2 states "The entity or any of the above criteria are likely to remain in existence for a time, i.e., the interest in the entity and its governmental characteristics are more than fleeting." 'Fleeting' may imply periods of one year or less to some and the Board considered how to clarify the term 'fleeting.' Ultimately, the Board decided terms such as 'fleeting' and 'temporary' implied a time limit.

A52. However, there may be instances where an intervention is longer than one year due to the extreme factors of the national crisis. In most instances, it is difficult to establish and meet a timeline for ending an intervention. In these instances, the focus continues to be on governance and protection, rather than maximizing profits or establishing new federal government lines of business. Although the actions may be longer than one year, the interventions are 'not expected to be permanent.' The Board established this 'non-permanent' expectation as a characteristic of disclosure entities rather than relying on 'temporary' or 'fleeting' to avoid the implication that a time limit could be established.

Component Reporting Entities

[57] CRS Report for Congress RL30533, *The Quasi Government: Hybrid Organizations with Both Government and Private Sector Legal Characteristics*

A53. The Board believes there should be consistency in treatment of organizations at the government-wide and the component reporting entity levels. The reasons for including entities in the government-wide entity GPFFR should be consistent with the reasons at the component reporting entity level. Further, classification as consolidation or disclosure entities would be consistent in government-wide and component reporting entity GPFFRs. The Board believes a single set of principles for inclusion and classification presented from the government-wide perspective provides for the desired consistency. This is appropriate and necessary because the government-wide reporting entity is the only federal reporting entity that is an independent economic entity.

A54. Nonetheless, implementation of these principles will involve the component reporting entities because the government-wide report is a consolidation of the reports provided by component reporting entities. Therefore, component reporting entities must identify and include in their GPFFR all consolidation and disclosure entities for which they are accountable so that both the component reporting entity GPFFR and government-wide GPFFR are complete.

A55. The Board believes that component reporting entities should identify consolidation and disclosure entities administratively assigned to the component reporting entity. Standards that are based on organization and accountability provide a more realistic view of how component reporting entities become accountable for organizations and how component entity boundaries are likely to be determined. The result will be component reporting entity GPFFR's that include all organizations for which the component reporting entity management (appointed officials) are expected to be accountable.

A56. Administrative assignments to component entities are typically made in policy documents such as laws, budget documents, regulations, or strategic plans. Ultimately, component reporting entities would identify and include in their GPFFR all consolidation and disclosure entities for which they are accountable so that both the component reporting entity and government-wide GPFFR would be complete.

A57. Administrative assignments can be identified by evaluating one or more of the following areas:

a. Scope of the Budget Process

b. Accountability Established Within a Component Entity

c. Misleading to Exclude and/or Misleading to Include

A58. Component reporting entities should develop processes to ensure organizations in each of these areas are identified, considered and assessed. Central agencies are anticipated to determine if there is a need for coordinated guidance to be developed to ensure government-wide consistency

A59. Although there may be a one-time review to ensure completeness and consistency, the Board believes this method is reasonably consistent with current practice. Further, a coordinated effort from the central agencies could promote a process to ensure the component reporting entities are performing the necessary procedures to capture the material organizations from their perspectives and also for consideration at the government-wide level. The effective date considered this and allowed sufficient time for a coordination of efforts.

GPFFR Consolidation and Disclosure

A60. As noted above, decisions about the government-wide GPFFR require determining what organizations are to be included in the reports and identifying appropriate means to present relevant information about organizations. The final determination of the presentation of financial information through consolidation or disclosure is based upon the results of two assessments—first if the organization is included and second, if those included organizations are classified as consolidation or disclosure entities.

A61. The **High Level Flowchart** at Appendix B to this ED is a useful tool in applying the principles established as it steps through this process. It is helpful in the assessment and applying the standards in order. It includes paragraph references to the ED and major decision points.

Consolidation entities

A62. The Statement provides that consolidation entities should apply SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*. In addition, it provides for the consolidation of the financial statements of consolidation entities so taxpayers and citizens may assess the financial position and the cost of operations of the federal government. Consolidation of financial information regarding the taxpayer supported activities, resources, and obligations where accountability rests with the Congress and/or the President ensures that the reporting objectives of SFFAC 1 are met.

Consolidation of FASB-based and FASAB-based Information

A63. The Board has considered the potential ramifications when some federal entities follow GAAP for nongovernmental entities promulgated by the private sector Financial Accounting Standards Board (FASB GAAP) and their information is consolidated with information based on FASAB standards. For example, federal government corporations, the U.S. Postal Service, certain component reporting entities of the U.S. Department of the Treasury, and some other entities in the executive and legislative branches have historically applied FASB GAAP and continue to do so. SFFAS 34 recognizes that "general purpose financial reports prepared in conformity with accounting standards issued by the FASB also may be regarded as in conformity with GAAP for those entities that have in the past issued such reports." SFFAS 34 also provides that a federal entity preparing audited financial statements for the first time may adopt FASB standards in the rare case that the needs of its primary users would be best met through the application of FASB standards. The acceptance of these practices raises the question of whether the information prepared under FASB standards may be consolidated with information prepared under FASAB standards in consolidated reports prepared by other component reporting entities and in the consolidated government-wide reporting entity.

A64. The Board has considered such issues on several occasions and provided concepts as follows:

> The reporting entities of which the components [preparing reports under FASB or regulatory accounting standards] are a part can issue consolidated, consolidating, or combining statements that include the components' financial information prepared in accordance with the other accounting standards. They need to be sensitive, however, to differences resulting from applying different accounting standards that could be material to the users of the reporting entity's financial statements. If these differences are material, the standards recommended by FASAB and issued by OMB and GAO should be applied. The components would need to provide any additional disclosures recommended by FASAB and included in the OMB issued standards that would not be required by the

other standards.[58] (SFFAC 2, Entity and Display, par. 78 (excerpt from section on "Financial Reporting For An Organizational Entity"))

A65. The Board determined in SFFAS 34 that FASB-based statements are acceptable in certain circumstances. While there are significant differences between FASB and FASAB standards, both standards result in accrual basis information and disclosures that aid users in understanding the information. Given the decisions made in SFFAS 34, members do not believe requiring a conversion of FASB-based information to FASAB-based information for consolidated financial reports of larger entities is justifiable.

A66. Users may be confused by the presentation of different amounts for a component in its own financial report and in the consolidated financial reports of larger entities; particularly when both amounts would be in accordance with GAAP for federal entities per SFFAS 34. In addition, conversion imposes a cost and it is not clear that the cost is justifiable based on benefits to the user. Therefore, this Statement proposes that amounts derived for component reporting entities in compliance with SFFAS 34 be consolidated without adjustment.

A67. However, if this leads to consolidation in a single line item of amounts measured differently due to differences between FASB and FASAB principles, then one would anticipate disclosures of the different accounting policies and the related amounts to aid the reader in understanding the information provided. The Board considered adopting requirements for such disclosures but believes that existing requirements and long-standing professional practices are sufficient.

Disclosure entities

A68. The Board believes consolidation of disclosure entities would not result in information meeting the basic qualitative characteristics of information in financial reports because it would not provide the most relevant, understandable, or consistent information. For example, for disclosure entities the Board believes consolidation may obscure the boundaries of the risks and rewards intended to be assumed or gained. Further, assets that are not available for purposes other than the specific business operation of the non-

[58] In October 1999, FASAB was recognized as the Rule 203 standards-setting body for the federal government. As such, FASAB now issues the standards, rather than issuing recommendations to OMB and GAO for issuance of the standards.

consolidated entity might be commingled with federal assets and liabilities not fully guaranteed by the federal government might be added to federal liabilities. For example, there may be certain funding streams—such as those related to monetary policy—that it makes sense to keep separate from fiscal policy to prevent unintended disruptions or distortions to the taxpayer financed financial statements.

A69. SFFAC 1 par. 49 states "…Federal accounting and financial reporting are shaped by, and need to respond to, the unique characteristics and environment of the federal government." SFFAC 1 par. 105 further explains "reports must accurately reflect the distinctive nature of the federal government and must provide information useful to the people, their elected representatives, and federal executives…" SFFAC 1 also provides the qualitative characteristics of information in financial reports, by identifying these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.[59]

A70. Flexibility in identifying needed information regarding disclosure entities is provided because the range of disclosure entities is broad and different information may need to be disclosed to meet the reporting objectives. Providing this flexibility allows the preparer to present information judged most necessary to meet reporting objectives while also providing an understanding of the potential effect of the relationship on the consolidation entity's financial statements.

Factors in Determining Disclosure Entity Disclosures

A71. Because of the flexibility needed regarding disclosures, preparers are provided a list of factors or guidance to assist in determining what disclosures to include. Materiality is an overarching consideration in financial reporting. Preparers should consider both qualitative and quantitative materiality in determining disclosure entity presentation and disclosure. Beyond materiality, the factors provided in the Statement assist in determining the nature and extent of information regarding a disclosure entity to be provided.

[59] SFFAC 1, par. 156

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Deleted: <#>One approach is to consider how to ensure that basic financial statements measure and communicate the risks and rewards assumed by the citizens.[60] Citizens have a clear interest in the risks and rewards assumed, but it is less clear that full consolidation provides the most relevant, understandable, or consistent measures of risks and rewards.¶
¶
<#>Par. 161 of SFFAC 1 discusses relevance as "…To be relevant, a logical relationship must exist between the information provided and the purpose for which it is needed. Information is relevant if it is capable of making a difference in a user's assessment of a problem, condition, or event. Relevance depends on the types of financial information needed by the various users to make decisions and to assess accountability." SFFAC 1 also provides that the concept of consistency in financial reporting extends to the determination of the financial reporting entity.[61] ¶

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A72. The factors are to be considered in the aggregate; no individual weight should be assigned or interpreted. The assessment of the appropriate disclosures should be made after considering all the factors.

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Disclosures

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A73. The Board recognizes that although the Statement provides flexibility in meeting the disclosure objectives, there is a wide variety of information listed as examples that may be disclosed to meet the intended objectives. Care should be taken to ensure the objectives are met, without producing unintended consequences. Preparers should keep in mind there are associated costs and potential audit implications with any information included in GPFFR. Incorporating by reference or including summary financial statements or summary financial information generally would result in an auditor being required to gain audit assurance on that information and thereby may result in additional audit costs.

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A74. The Board believes any financial information about disclosure entities in the government-wide GPFFR should be based on accrual basis standards specific to the type of entity while minimizing additional costs on the disclosure entity. Therefore, there will be instances where information about disclosure entities is based on reporting periods that differ from the GPFFR reporting period. The Board agreed that if disclosure entities have a different reporting period than the government-wide GPFFR, disclosure of information from a reporting period ending within the government-wide reporting entity's reporting period is acceptable. The Board performed outreach on this issue to the audit community and to the federal entity task force. Generally, the feedback supported this approach.

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A75. However, due to the fact there could be a large time lag, there should be a provision for disclosing significant changes in the information as a result of events occurring after the issuance of the disclosure entity's audited financial statements and before the issuance of the reporting entity's audited financial statements for a later fiscal year end. The Board notes this would only be necessary if a disclosure entity's summarized financial statements or summarized financial information were presented. Otherwise normal transactions would be captured throughout the year so this would be a somewhat narrowed focus.

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A76. The Board is especially concerned with the interpretation by the users and preparers regarding the proposed ED requirements for disclosure entities and ultimately how they would affect the display and disclosures. The Board believes this would be an important consideration during deliberations on the ED and invited the assistance of the Department of the Treasury and a potential included organization in preparing a draft Illustration of a disclosure based on the draft requirements.

A77. Although the Board believed some enhancement of the draft standards was in order to encourage concise and transparent disclosures, the Board agreed the inclusion principles were appropriate. Further, the flexibility provided within the disclosure requirements, along with the factors to consider, were preferable to prescribing information required regarding specific entities. The Board noted the need to emphasize the aggregation of information, referencing other disclosures when possible, additional focus on risk and other enhancements to the draft disclosures. This need arose because of the complexity of the relationships being described, transactions affecting multiple assets and liabilities being reported, and the desirability of an integrated set of disclosures. The Board subsequently modified the draft disclosure requirements to emphasize integration of disclosures.

Related Party

A78. The Board determined it should define 'related party' and address it within this Statement for several reasons. Related party reporting is such a fundamental notion within GAAP and the auditing standards that addressing how related party concepts apply in the federal domain is important. Absent clear related party concepts and concerns in the federal domain, the Board believes the private sector concepts would be applied by default.

A79. The provision incorporates those parties with an established relationship that involves significant influence. Because of the extent of the federal government's relationships – whether already established or implied – the standards rely heavily on listing parties to be included and excluded. In addition, the proposal provides room for judgment by incorporating a misleading to exclude provision.

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A80. Further, one cannot anticipate all types of relationships the federal government may have or might have in the future that should be reported. The related party category is needed to provide for disclosure of those organizations that are not included under the inclusion principles but where there is an existing relationship of significant influence.

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A81. Component reporting entities of a single controlling entity are generally subject to related party reporting requirements in other domains. So,the Board discussed whether jointly controlled component reporting entities should disclose information about their relationships. Presently, component reporting entities are required by OMB guidance to state in the management's discussion and analysis section that: "The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity." In addition, existing standards require recognition of inter-entity costs to ensure that cost information is not misstated as a result of relationships between component reporting entities. While members noted that readers may need additional contextual information to understand what these complex relationships imply about component reporting entity information, they preferred that OMB explore options for additional guidance through Circular A-136, *Financial Reporting Requirements,* so that it is integrated with existing disclosure requirements. Addressing additional disclosures in this Statement would likely expand its scope into areas adequately addressed in established practice.

Proposed Amendments to SFFAC 2

A82. The purpose of this section of the Statement is to propose amendments to Statement of Federal Financial Accounting Concepts (SFFAC) 2, *Entity and Display*. The Statement provides a description of the change to SFFAC 2 and an explanation as to why the change is being made. Most of the conforming changes are rescissions that result from movement of criteria for determining what organizations are required to be included in the federal reporting entity's GPFFR from a concepts statement to standards statement.

Deleted: and are a result of concepts that go beyond conceptual guidance and appear to establish standards within a concepts statement. Deleting this will avoid any confusion regarding the role of the inclusion principles presented in the draft standards without creating a void in concepts. ¶
Minimal conforming changes have been proposed to SFFAC 2

A83. Paragraphs 54—77 and 79 – 112 address concepts outside the scope of this Statement and are not amended.

A84. In addition, paragraphs 11-37 remain as is with no proposed changes because the Board believes these paragraphs provide the conceptual underpinning for understanding the structure of the federal government and how this relates to reporting entities for general purpose federal financial reporting. Although there may be some small differences in terminology in those paragraphs, the Board did not believe they were significant enough to warrant a rewrite of the section or individual paragraphs.

A85. Paragraphs 47-50 identify certain entities or types of entities (the Federal Reserve System, Government Sponsored Enterprises and Bailout Entities) that could be included in the government-wide reporting entity based on the SFFAC 2 concepts but that should not be included.[63] This Statement establishes principles to ensure users of GPFFR are provided comprehensive financial information while recognizing the complexity of the federal government and its relationships with varied organizations. The new principles can be applied to the entities previously excluded and conclusions reached to include the entities—either as consolidation or disclosure entities—or to continue to exclude the entities. SFFAC 2 is being amended to ensure that concepts provide a framework for standards-setting but do not themselves establish standards by listing specific exclusions.

[63] SFFAC 2, *Entity and Display*, par. 47-50.

Appendix B: FLOWCHART

Appendix C: Illustrations

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Appendix D: Abbreviations

CFR	Consolidated Financial Report
DOL	U.S. Department of Labor
ED	Exposure Draft
FASAB	Federal Accounting Standards Advisory Board
FASB	Financial Accounting Standards Board
GAAP	Generally Accepted Accounting Principles
GPFFR	General Purpose Federal Financial Reports
OAI	Other Accompanying Information
OMB	Office of Management and Budget
RSI	Required Supplementary Information
SFFAC	Statement of Federal Financial Accounting Concepts
SFFAS	Statement of Federal Financial Accounting Standards
U.S.	United States

Appendix E: Glossary

Component Reporting Entity "Component reporting entity" is used broadly to refer to a reporting entity within a larger reporting entity.[64] Examples of component reporting entities include entities such as executive departments, independent agencies, government corporations, legislative agencies, and federal courts. Component reporting entities would also include sub-components (those components included in the GPFFR of a larger reporting entity) that may themselves prepare GPFFRs. One example is a bureau that is within a larger department that prepares its own standalone GPFFR.

Conservatorship A conservatorship is the legal process in which a person or entity is appointed to establish control and oversight of a Company to put it in a sound and solvent condition. In a conservatorship, the powers of the Company's directors, officers, and shareholders are transferred to the designated Conservator.[65]

Control with risk of loss or expectation of benefit Control with risk of loss or expectation of benefit is the power to impose will on and/or govern the financial and/or operating policies of another organization with the potential to be obligated to provide financial support or assume financial obligations or to obtain financial resources or non-financial benefits.[66]

Disclosures Reporting information in notes or narrative regarded as an integral part of the basic financial statement.

Federally Funded Research and Development Center Federally Funded Research and Development Center (FFRDC) is a government-funded entity that has a long-term contractual relationship with one or more federal agencies.[67] FFRDCs can be privately owned or government-owned, and they serve to meet the long-term research and development needs of federal agencies that could not otherwise be met as effectively in-house or through existing contractors. 49 Fed. Reg. at 14,464; 48 C.F.R. § 35.017(a). FFRDCs are established either specifically in statute or under the statutory authority of

[64] The larger reporting entity could be the government-wide reporting entity or another component reporting entity.
[65] Federal Housing Finance Agency Fact Sheet, *Questions and Answers on Conservatorship*
[66] For example, a non-financial benefit would be one where the federal government benefits from a service being provided to it or on its behalf.
[67] The OFPP and FAR policies for FFRDCs apply to executive agencies, which includes "an executive department, a military department, or any independent establishment within the meaning of 5 U.S.C. 101, 102, and 104(1), respectively, and any wholly owned Government corporation within the meaning of 31 U.S.C. § 9101." 48 C.F.R. § 2.101; *see also* 5 U.S.C. § 403.

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agencies to enter into contracts, which can be inherent or specific authority, and are used to perform research and development and related tasks.

General Purpose Federal Financial Reports General purpose federal financial reports (GPFFR) is used throughout this Statement as a generic term to refer to the report that contains the reporting entity's financial statements that are prepared pursuant to generally accepted accounting principles. In the federal government, the report for the U.S. government-wide reporting entity is known as the Financial Report of the U.S. Government and for component reporting entities it is usually called the Performance and Accountability Report, the Agency Financial Report, or the Annual Management Report.

Government-wide Reporting Entity The government-wide reporting entity's GPFFR includes all organizations for which the Congress and/or the President are accountable based on principles established in this Statement.

Receivership Receivership is the legal procedure for winding down the affairs of an insolvent institution.[68]

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Related Party Related parties are not controlled or owned by the federal government. Organizations are considered to be related if the relationship or one party to the relationship has the ability to exercise significant influence over the other party in making financial and operating decisions.

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Reporting Entity Reporting entities are entities that issue a GPFFR because either there is a statutory or administrative requirement to prepare a GPFFR or they choose to prepare one. The term "reporting entity" may refer to either the government-wide reporting entity or a component reporting entity (see definitions below).

Statement of Federal Financial Accounting Concepts (SFFAC) 2 provides criteria for an entity to be a reporting entity.[69] The criteria focus on whether an entity should issue GPFFRs and are that a reporting entity's:

a. management is responsible for controlling and deploying resources, producing outputs and outcomes, and executing the budget or a portion

[68] *Managing the Crisis: The FDIC and RTC Experience*, Appendix B - List of Abbreviations and Glossary of Terms; available online at http://www.fdic.gov/bank/historical/managing/; last accessed October 11, 2012.

[69] SFFAC 2, par. 29-37, provides a discussion on Identifying the Reporting Entity for General Purpose Financial Reporting.

thereof (assuming that the entity is included in the budget), and is held accountable for the entity's performance.

b. financial statements would provide a meaningful representation of operations and financial condition.

c. financial information could be used by interested parties to help them make resource allocation and other decisions and hold the entity accountable.

Appendix F- Federal Reporting Entity Task Force Members

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Owen Barwell, (formerly of) Department of Energy
Lieutenant Colonel Richard Brady, USMC DOD
Terry Bowie, (formerly of) NASA
Naresh Chopra, Department of Labor
Tom Daxon, Former Oklahoma State Auditor
Ann Davis, US Department of Treasury
Lynda Downing, GAO
Abe Dymond, GAO
Joel Grover, US Department of Treasury, OIG
Mark Hadley, CBO
Regina Kearney, OMB
Karen Kelbly, NCUA
Dan Kovlak, KPMG
Rick Loyd, Department of Energy
Ned Maguire, (formerly of) Office of the Dir. of National Intelligence, OIG
Sam Papenfuss, CBO
Reginald Royster, HUD
Fred Selby, US Department of Treasury, OFS
Gary Solamon, Department of Commerce, Bureau of Economic Analysis
Sandy Van Booven, National Reconnaissance Office (CIA)
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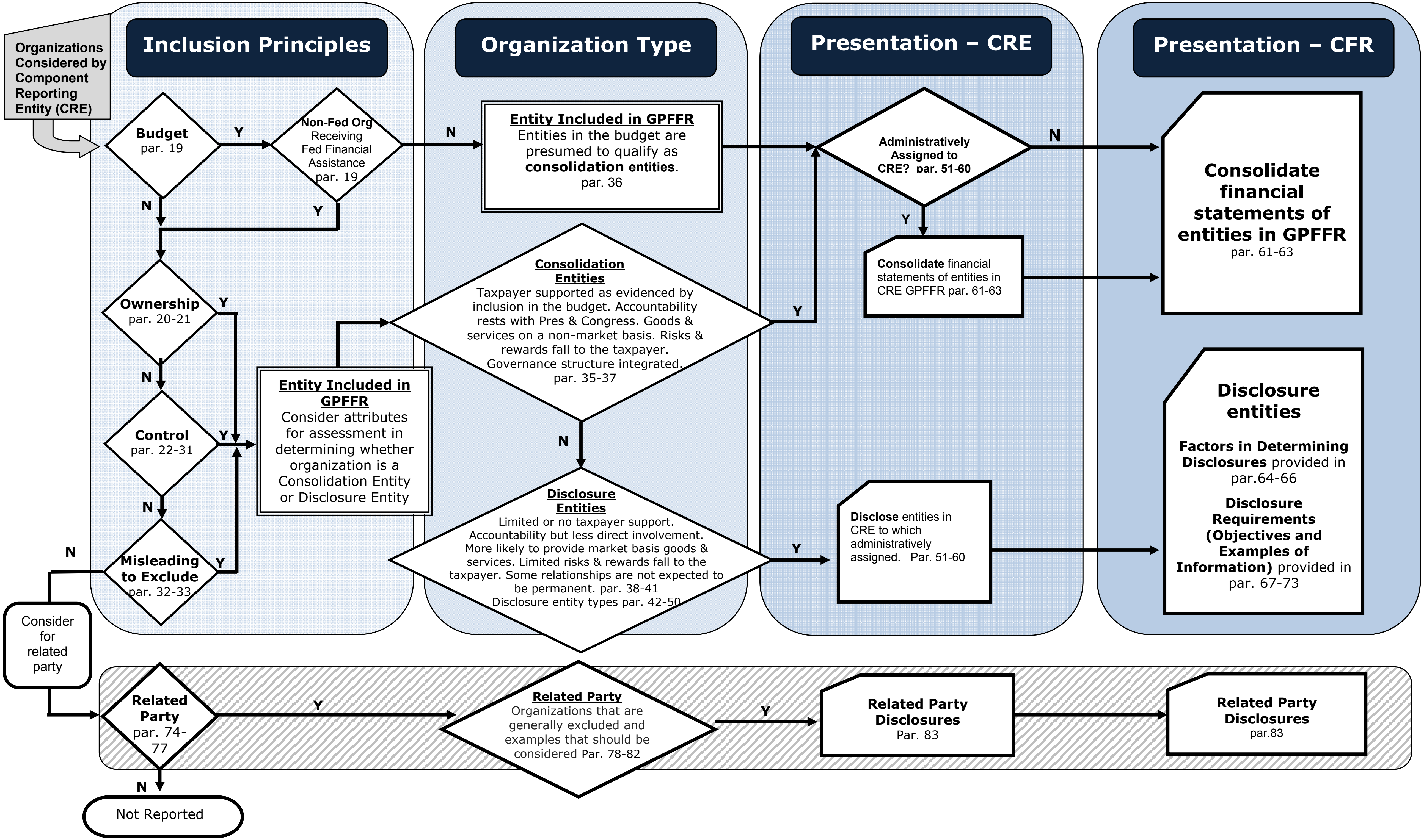
FLOW CHART (Appendix B)



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Preamble

These illustrations demonstrate how the provisions of the proposed standards could be applied to organizations given simplified hypothetical circumstances. They are for illustrative purposes and are nonauthoritative. They do not:

1. represent actual entities.
2. provide a thorough analysis of all the facts and circumstances that are needed to reach a conclusion in practice.
3. indicate a preferred method of analyzing facts and circumstances.
4. substitute for the application of professional judgment to actual facts and circumstances.

These illustrations follow the sequence presented in the decision flowchart in Appendix B of the ED, *Identifying Organizations to Include in GPFFR and Related Presentation Requirements*. All tentative conclusions are based primarily on the hypothetical circumstances presented. In most illustrations the tentative conclusions refer to consideration of other factors by management and the auditor. This reference is included to emphasize that, in practice, consideration of all relevant facts and circumstances would be needed to reach conclusions. The reader should assume that the general reference to ‘other factors’ means that such factors, in aggregate, supported the conclusions implied by the necessarily limited assumed facts and circumstances presented in each illustration.

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Application of the proposed standards to actual entities requires consideration of the circumstances specific to each entity and the exercise of professional judgment. Although the limited assumed facts and circumstances presented in the illustrations may be similar to situations at a particular reporting entity, they should not be used in practice as a substitute for a complete and thorough consideration of all of the relevant facts and circumstances, which may lead to a conclusion different from the tentative conclusions in these illustrations. For example, the illustrations make certain assumptions that, in practice, require judgment of the specific facts and circumstances to make appropriate determinations.

All of the illustrations discuss administrative assignments to component reporting entities where there is only one component reporting entity relationship described. In reality, more than one component reporting entity may have a relationship with the illustrative entity. In such cases, additional information would need to be considered to determine whether other administrative assignments exist.

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ABC Department

(In the Budget—Consolidation Entity)

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Assumed Facts and Circumstances

Congress established ABC Department (ABC), a federal organization, to promote entrepreneurship and innovation as a means to address national economic and environmental challenges. Provisions that govern ABC are generally prescribed in legislation and ABC accomplishes its mission through the activities of various bureaus, grants to research institutions, and contracts with universities and not-for-profit organizations.

The executive leadership of ABC consists of a secretary, deputy secretary, and three assistant secretaries. The President nominates and the Senate confirms each of these officials. These officials serve at the pleasure of the President. ABC is subject to all laws and regulations applicable to executive branch agencies.

ABC relies on appropriated public funds to conduct its mission and is included in the *Budget of the United States Government: Analytical Perspectives – Supplemental Materials schedule Federal Programs by Agency and Account* (Budget). The President and the Congress consider ABC's requests for resources and determine the amount that should be budgeted to provide services. Furthermore, ABC is not considered to be a non-federal organization receiving federal financial assistance.

Tentative Conclusions

Based on the assumed facts and circumstances, management determined and the auditor concurred that ABC should be included in the government-wide GPFFR because it (1) meets the first of the three inclusion principles (being listed in the budget) and (2) is not a non-federal organization receiving federal financial assistance.

Classification as a Consolidation or Disclosure Entity

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Further, because it is listed in the budget, ABC is presumed to qualify as a consolidation entity assuming no information to the contrary. In this example, management determined and the auditor concurred that there were no facts contradicting the assumption that ABC is a consolidation entity. As a consolidation entity, ABC's financial statements should be consolidated in the government-wide GPFFR.

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Administrative Assignments

The assumed facts and circumstances do not indicate ABC should be consolidated with another component reporting entity. Further consideration of ABC's relationships with other consolidation entities would be needed to determine if ABC has been administratively assigned to another component reporting entity. Further consideration would also be needed to identify any consolidation or disclosure entities administratively assigned to ABC.

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Epsilon Corporation

(In the Budget – Consolidation Entity)

Assumed Facts and Circumstances

The Congress and the President established Epsilon Corporation as an independent government corporation to insure consumer funds placed in trust with certain types of institutions. Federal legislation established provisions that govern Epsilon's activities. Epsilon is governed by a seven member board of directors and each board member is appointed by the President and confirmed by the Senate. The Congress monitors Epsilon's activities by conducting hearings on Epsilon's programs and requesting Government Accountability Office (GAO) and Office of Inspector General (OIG) audits.

Epsilon is listed in the Budget and receives its funding based on legislation permitting it to receive and spend premiums from the institutions it insures. Legislation limits how Epsilon can invest proceeds from premiums and, to help ensure that Epsilon remains financially viable, legislation requires Epsilon to have a reserve fund. The board of directors determines the level of the reserve fund. If Epsilon encounters a shortfall, the entity may borrow a limited amount from the U.S. Department of the Treasury, but any additional funding requirements must be obtained from premium assessments.

Epsilon is required to periodically report to the Congress and the President on matters such as:

- Program performance results
- Financial position, results of operations, and cash flows
- Adequacy of internal controls and systems

Furthermore, Epsilon is not considered to be a non-federal organization receiving federal financial assistance.

Tentative Conclusions

Based on the assumed facts and circumstances, management determined and the auditor concurred that Epsilon Corporation should be included in the government-wide GPFFR because it meets the first of the three inclusion principles (being listed in the budget) and is not a non-federal organization receiving federal financial assistance.

Classification as a Consolidation or Disclosure Entity

Further, because it is listed in the budget, Epsilon is presumed to qualify as a consolidation entity assuming no information to the contrary. In this example, management determined and the auditor concurred that there were no facts rebutting or contradicting the assumption that Epsilon is a consolidation entity. As a consolidation entity, Epsilon's financial statements should be consolidated in the government-wide GPFFR

Administrative Assignments

There is no information included in the assumed facts and circumstances indicating that Epsilon should be consolidated with another component reporting entity. Further consideration of Epsilon's relationships with other consolidation entities would be needed to determine if Epsilon has been administratively assigned to another component reporting entity or has had consolidation entities administratively assigned to it. Also, further

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consideration would be needed to identify any disclosure entities administratively assigned to Epsilon for which disclosures are needed.

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Sigma Association

(Control based on Persuasive Indicator - Disclosure Entity (financially independent))

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Assumed Facts and Circumstances

The Congress and the President established Sigma Association (Sigma) as a not-for-profit, non-taxpayer funded organization to market innovative U.S. agricultural technology worldwide and to respond to any claims of damage arising from new technology. The fundamental purpose of the corporation is specified in legislation and its mission statement is "to open new markets for U.S. agricultural technology through a cooperative marketing strategy and risk-sharing approach for market participants."

Sigma is governed by a ten-member board of directors. Five members are appointed by the President and confirmed by the Senate. Four members are elected by industry members. The Secretary of Agriculture (or his/her designee) serves as a voting ex-officio member of the board. No more than three of the appointed members may be from the same political party. Board members serve seven-year terms and can only be removed for cause (meaning they may not be removed for policy decisions). Also, Congress monitors Sigma's activities by conducting hearings on Sigma's programs and requesting GAO audits.

Sigma is financed by fees imposed on industry members. Sigma's board of directors must establish an annual budget and legislation limits how Sigma can invest proceeds from fees and, to help ensure that Sigma remains financially viable, legislation requires Sigma to have a reserve fund. The board of directors determines the level of the reserve fund after considering input from industry members. If Sigma encounters a shortfall, it may borrow a limited amount from the U.S. Department of the Treasury (Treasury), but any additional funding requirements must be obtained from future fee assessments on industry members.

Tentative Conclusions

Based on the assumed facts and circumstances, and other considerations, management determined and the auditor concurred that Sigma should be included in the government-wide GPFFR because Sigma meets the third inclusion principle (control with expected benefits or risk of loss). Indicators that the federal government can control Sigma are that the Congress and the President (1) established its fundamental purpose and mission through legislation and (2) appoint a majority of the members of its board of directors (its governing body). Each of these facts individually would be sufficient to indicate control such that Sigma would be included.

Classification as a Consolidation or Disclosure Entity

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For this illustration, management determined and the auditor concurred that, based on the assumed facts and circumstances as well as other considerations not described in the illustrations, Sigma should be reported as a disclosure entity because it is a financially independent entity. Management and the auditor considered the assumed facts and circumstances presented below in the aggregate, weighed them against other considerations, and used professional judgment.

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Evidence suggesting that it is a disclosure entity includes:

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1. Taxpayer support is not provided for ongoing operations.

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2. The corporation is relatively financially independent because it is primarily funded from a source other than appropriations. Its budget and fees are not subject to Congressional or Presidential approval.
3. Seven-year terms for directors and their not being subject to removal for policy decisions indicate a higher degree of autonomy than executive branch appointees. This governance structure vests greater decision making authority with the board while insulating it from political influence. As a result, Congressional and Presidential oversight is less direct since they are not involved in decisions such as the level of reserves needed.
4. While Sigma is permitted to borrow from the Treasury, such borrowing is limited. This means risks to the taxpayer are limited. Instead, Sigma is expected to maintain its operations and meet its liabilities with revenues received from sources outside of the federal government.

Evidence suggesting that Sigma may be a consolidation entity includes:

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1. Accountability rests with the President and the Senate who appoint and confirm, respectively, members of the board of directors as well as establish organizational authorities in legislation.
2. Sigma provides a service that is not available from market participants. Its fees are adjusted to recover losses rather to respond to market influences. Hence, its fees are not market based.

Administrative Assignment

Because each disclosure entity must be reported by at least one consolidation entity, management considered whether Sigma has been administratively assigned to the Department of Agriculture. Evidence suggesting administrative assignment to the Department of Agriculture includes that the secretary serves as an ex-officio member of the board.

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As a result, management determined and the auditor concurred that the Department of Agriculture should disclose information regarding Sigma in its GPFFR. If Sigma is also administratively assigned to other component reporting entities, then those entities should also consider the need to disclose information in their GPFFRs.

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Scholars University

(Not Included)

<u>Assumed Facts and Circumstances</u>

The Congress and the President chartered Scholars University as a small, private, independent, not-for-profit educational institution and legislation describes the mission of the university. The legislation also indicates that the university is not an instrumentality of the federal government and that the federal government does not assume any liabilities of the university.

Scholars University is governed by a 29-member board of trustees. The Secretary of Education is an ex-officio member of the board and the remaining members are elected by the board for three-year terms. The board controls and directs the university's affairs such as determining the university's tuition and fee structure, adding or removing colleges within the university, and establishing new research institutions.

To support its mission, Scholars University receives most of its revenue from student tuitions and fees, and private contributions. The university receives appropriations to support some of its academic programs. The university is listed in the Budget under a Department of Education program because an amount is appropriated for Scholars University each year. Although the appropriations discuss limitations on how the funds may be used, the university generally has discretion over how it chooses to allocate funds for its academic programs and construction activities.

<u>Tentative Conclusions</u>

Based on the assumed facts and circumstances and other information, management determined and the auditor concurred that Scholars University should not be included in the government-wide GPFFR. Although listed in the Budget, management asserts that Scholars University is a non-federal organization receiving federal financial assistance in the form of a grant. Any non-federal organization listed in the budget should be assessed against the other two principles. So, management must determine if the other inclusion principles are met or if it would be misleading to exclude the university.

The initial analysis is summarized below:

- <u>Ownership</u> – The Congress and the President chartered Scholars University as a private, independent entity. There is no evidence that the federal government has an ownership interest in the university.

- <u>Control</u> - Based on the assumptions presented, the persuasive indicators of control have not been met. While the federal government chartered Scholars University, the standards provide that further indicators of control must be present to conclude that the entity is controlled. The remaining persuasive indicators—appointing or removing a majority of the governing board members, establishing financial and operating policies, and dissolving the university and having access to its assets—are not met. The available facts and circumstances suggest that Scholars is not controlled. [Note, however, for brevity this illustration does not present an analysis of indicators of control that in the aggregate may reveal that Scholars is controlled. Such an analysis may be needed in practice.]

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- Misleading to exclude - Scholars University is a small not-for-profit that is listed in the Budget solely as a program within the Department of Education. Management determined and the auditors concurred that it is both quantitatively and qualitatively immaterial. Also, there were no other facts and circumstances that would suggest that Scholars University should be included in the GPFFR. As a result, it would not be misleading to exclude.

Based on the assumed facts and circumstances and other considerations, management determined and the auditor concurred that Scholars University should not be included in the government-wide GPFFR.

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Education Research Institute (ERI)

(Control based on Persuasive Indicator – Consolidation Entity)

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Assumed Facts and Circumstances

The purpose of the ERI is to assist state and local officials in making informed decisions regarding effective education methods. ERI was established by the Congress and the President through a public law specifying the organization's:

- status as a tax exempt not-for-profit,
- purpose and duties,
- governance structure,
- sources of financing, and
- reporting requirements.

The public law establishing ERI requires reauthorization of its operations every five years. If the Congress and the President do not authorize continued operation, ERI must cease operations and distribute its net assets to a successor organization designated by the federal government. If ERI is unable to satisfy its liabilities prior to dissolution, the federal government will assume its liabilities.

ERI is governed by a seven-member board of directors; five of whom are voting. Two members are specific federal officials within the Department of Education who serve part-time and do not having voting rights. The remaining five serve full-time and are appointed by the Association of Local School Boards and serve six-year terms. One of these five members is elected by the board to serve as chairperson.

The legislation creating ERI designates funding of $1 per elementary school student per year to be made available from the general fund of the U.S. Treasury to the ERI trust fund. An annual transfer to ERI is not listed in the Budget but is included in the Department of Education's Congressional Budget Justification. The board of directors is authorized to establish an annual budget not to exceed the amounts available in the trust fund. ERI may fund up to 25% of its annual budget through donations but may not use federal funds to solicit donations.

The Department of Education approves the ERI annual budget. The department also reports information related to ERI activities in its annual performance report and Congressional Budget Justification.

ERI must provide annually an audited financial report to the Department of Education and relevant Congressional committees.

Tentative Conclusions

Based on the assumed facts and circumstances and other considerations, management determined and the auditor concurred that ERI should be included in the government-wide GPFFR because the third inclusion principle (control) is met. A persuasive indicator of control exists because the federal government can unilaterally dissolve the organization and have access to its assets and responsibility for its liabilities.

Classification as a Consolidation or Disclosure Entity

For this illustration, management determined and the auditor concurred that, based on the assumed facts and circumstances as well as other considerations not described in the illustrations, ERI should be reported as a consolidation entity. In arriving at this conclusion, management and the auditor considered the assumed facts and circumstances presented below in the aggregate and, finding no other facts that in the aggregate contradict these, used professional judgment to determine that ERI is a consolidation entity.

Evidence suggesting that ERI is a consolidation entity includes:

1. It is primarily financed by taxpayers.
2. Taxpayers have assumed the risks associated with ERI's liabilities.
3. The purpose of ERI is to assist state and local officials by providing consultation services on a non-market basis.
4. ERI's annual budget is approved by the Department of Education and the Department also provides information related to ERI activities in its annual performance report and Congressional Budget Justification. These activities show that elected officials, acting with and through politically appointed officials, make decisions regarding ERI's budget.

Evidence suggesting that ERI is a disclosure entity includes:

1. A majority of the members of the board of directors is appointed by non-federal officials.
2. ERI is able to access donations to sustain some of its operations.

Administrative Assignment

The Department of Education should consider whether or not ERI is administratively assigned to it. Evidence that indicates ERI is administratively assigned includes Education's participation in ERI's budgetary process and inclusion of information regarding ERI in its own Congressional Budget Justification. Having considered the above information and other available evidence, the Department of Education determined and its auditor concurred that it should consolidate ERI's financial statements in its GPFFR.

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Mediation Corporation

(Control based on Indicators in the Aggregate –Disclosure Entity)

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Assumed Facts and Circumstances

Mediation was established as a 501(c)(3) non-member not-for-profit organization through a public law specifying the organization's:

- status and operating location,
- purpose and duties,
- governance structure,
- sources of financing, and
- reporting requirements.

The purpose of Mediation is to ensure that low-income individuals have access to mediation services to resolve non-criminal legal disputes. An assigned duty is to develop and maintain a network of state and local government organizations to deliver services financed by grants. Network members may raise funds to finance delivery of services through taxes, donations, and other grants without limitation.

The governing board comprises 13 members including Mediation's executive secretary. The President nominates candidates to fill the board member positions. A panel of local government officials participating in the network selects new members of the governing board from among the nominees. No more than seven members may be affiliated with the same political party. The members elect their chairperson from among the members. The President appoints the executive secretary and the Senate confirms appointment. The executive secretary's term is fifteen years during which the President may only remove the appointee for cause.

Mediation is financed by an annual appropriation, interest earnings, and grants from any public or private grant making organization. Grants must not finance more than 20% of its annual budget. The U.S. Attorney General approves the annual budget. Any liabilities incurred by Mediation must be settled from its assets and are not backed by the full faith and credit of the U. S. Government.

An annual appropriation is provided in the federal budget for "Grants to the Mediation Corporation." The appropriation is made to the Department of Justice which transfers budget authority to Mediation. Mediation manages its cash balances similar to other not-for-profits and may retain any interest earned on unspent funds. In addition, it may apply for and receive grants from any grant making organization—public or private—subject to the 20% limitation.

The public law creating Mediation requires it to make annual audited financial reports publicly available. Mediation also files annual tax returns with the Internal Revenue Service. Furthermore, Mediation is considered to be a non-federal organization receiving federal financial assistance.

Tentative Conclusions

Although Mediation is listed in the Budget, it is a non-federal organization receiving federal financial assistance. To determine if Mediation should be included in the government-wide GPFFR, management considered the remaining inclusion principles—ownership and control. It is unclear, based on the assumed facts and circumstances, whether Mediation is owned by the federal government. Therefore, management must consider the control indicators to determine if the third inclusion principle is met. None of the persuasive indicators of control are present based on the assumed facts and circumstances so considerable professional judgment is required to determine whether – in the aggregate – the indicators provide evidence of control. The indicators suggesting federal government control over Mediation include:

1. The federal government provides significant input regarding selection of the entity's governing board members since a selection can only be made from among candidates identified by the President.
2. The President appoints a key executive – the executive secretary – and may remove him or her for cause.
3. Federal law restricts Mediation's capacity to generate revenues since only appropriations, interest earned, and grants may be used. In addition, only 20% of its annual needs may be met through grants.
4. The U.S. Attorney General approves the annual budget.
5. Federal law requires annual audited financial reports.
6. Federal law directs Mediation to work through a network of government agencies to provide services.

Based on the assumed facts and circumstances and other considerations, and using professional judgment, management determined and the auditor concurred that Mediation should be included in the government-wide GPFFR.

Classification as a Consolidation or Disclosure Entity

For this illustration, management determined and the auditor concurred that, based on the assumed facts and circumstances as well as other considerations not described in the illustrations, Mediation should be reported as a disclosure entity. In arriving at this conclusion, management and the auditor considered the assumed facts and circumstances presented below in the aggregate and, finding no other facts that in the aggregate contradict these, used professional judgment to determine that Mediation is a disclosure entity.

Evidence suggesting that Mediation is a consolidation entity includes:

1. It is primarily funded by taxpayers.
2. Elected officials determine Mediation's budget, because at least 80% of its funding is appropriated to Justice. In addition, an appointed federal official, the U.S. Attorney General, approves Mediation's annual budget.

Evidence suggesting that Mediation is a disclosure entity includes:

1. Members of its governing body are selected by non-federal officials, serve longer terms than political appointees, must include members from different political parties, and may only be removed for cause. These conditions insulate the governing body from political influence.

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2. Mediation has some access to non-federal funding through grants and its network of service providers is free to access non-federal funding for service delivery (subject to the 20% limitation).
3. Taxpayers have not assumed risks related to Mediation's liabilities.

Administrative Assignments

The Department of Justice should consider whether or not Mediation is administratively assigned to it. Evidence that indicates it is administratively assigned includes the Department of Justice's participation in Mediation's budgetary process. After considering the above and other factors, and using professional judgment, management at the Department of Justice determined and the auditor concurred that disclosures regarding Mediation should be presented in its GPFFR.

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Bicycle America, Inc. (Scenario A)

(Not Included)

Assumed Facts and Circumstances

Individual bicycle shop owners determined that a nation-wide network of shops and trails was needed to encourage greater reliance on bicycles for transportation and invested in a new corporation, Bicycle America. BA's mission was to create a coast-to-coast network and ensure wide access to bicycling. Shares in the venture are held by local bicycle shops in all major cities.

BA is governed by a board of directors. The board controls and directs the organization's affairs and interests. Board members are elected by the shareholders to serve three-year terms.

Until recently, BA was able to finance its operations from user fees. A recent lawsuit led to serious financial challenges and cash was unavailable to meet pressing needs. Absent a cash inflow, BA was considering closing the trails. Due to exceptional citizen reliance on the trails for transportation and recreation, the federal government intervened and enacted legislation to provide funding.

The federal government provided a short-term loan to BA. The federal financial intervention to preserve BA was not separately identified in the Budget, but was part of a larger federal program within the Department of Transportation.

The funding legislation also established a temporary advisory committee to monitor BA's financial condition and inform Congress of potential issues that may warrant additional actions. In addition, the advisory committee will develop a plan to aid BA in returning to financial solvency and refinancing the short-term loan.

Tentative Conclusions

Based on the assumed facts and circumstances and other considerations, management determined and the auditor concurred that BA should not be included in the government-wide GPFFR. Specifically, BA is not listed in the Budget. Further, based on the available information and other considerations, management determined and the auditor concurred BA does not meet either the remaining ownership or control inclusion principle because BA continues to be owned by common shareholders and governed by the existing board of directors. The advisory committee offers advice to the Congress and does not have authority to direct BA to act.

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Bicycle America, Inc. (Scenario B)

(Ownership – Disclosure Entity (Intervention))

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Assumed Facts and Circumstances

Same as above except that in addition to the actions in Scenario A above, the federal government received shares that carry 51% of the voting rights of BA common stock and the advisory committee will develop a plan to sell the shares.

Tentative Conclusions

Based on the changed assumptions and no information to the contrary, and using professional judgment, management determined and the auditor concurred that BA should be included in the government-wide GPFFR. When the federal government holds a majority ownership interest, albeit temporary, the owned entity should be included in the government-wide GPFFR.

Classification as a Consolidation or Disclosure Entity

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The available facts and circumstances indicate that the federal government's involvement with BA is an intervention not expected to be permanent. Based on the assumed facts and circumstances and other considerations, management determined and the auditor concurred that BA should be reported as a disclosure entity because ownership resulted from an intervention. The initial determination would need to be evaluated periodically to determine if the intervention continues to be intended to be temporary.

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Administrative Assignments

Department of Transportation was assigned responsibility for transferring funds to BA which indicates an administrative assignment. As a result, management determined and their auditor concurred that the department should disclose information regarding BA in its GPFFR. If BA is also administratively assigned to other component reporting entities, then those entities should also disclose information in their GPFFRs.

Chatham Laboratory

(Control based on Persuasive Indicator – Consolidation Entity (FFRDC))

Assumed Facts and Circumstances

Federal Department of ABC (ABC) organized Chatham Laboratory as a federally funded research and development center (FFRDC) to conduct specialized engineering research that supports ABC's mission related to infrastructure and leads to improved services. As specified in the agreement, ABC provides the physical capital and ongoing funding for the FFRDC and sets research goals for Chatham.

ABC selects a contractor to operate Chatham and conduct research consistent with the established goals. ABC is not involved in the day-to-day operations of Chatham. ABC routinely evaluates Chatham's performance and maintains a research office to review strategic plans, consider progress, and serve as a liaison to other federal institutions. ABC reports on Chatham's efforts in its own performance reports.

Chatham operations are funded entirely through appropriations provided to ABC. ABC identifies Chatham in its Congressional Budget Justification but Chatham is not specifically identified in the President's Budget. Instead, amounts for Chatham are included in a larger research program which makes payments to the contractor consistent with the terms of the contract. Chatham's contract operator must submit financial and performance reports to ABC periodically. All Chatham assets belong to the federal government and the results of Chatham research are the property of the federal government. In addition, ABC would be responsible for liabilities arising from use of the facilities to conduct research such as environmental cleanup liabilities. ABC is also responsible for employee benefits in the event Chatham operations are terminated.

Tentative Conclusions

Based on the assumptions and other considerations, management determined and the auditor concurred that Chatham should be included in the government-wide GPFFR. While contracting for the operation of Chatham, officials at ABC also act as the governing body by establishing the purpose and mission of Chatham. Further, ABC continues in this role through its involvement in Chatham's strategic planning and monitoring of performance. Establishing the purpose and mission of an organization is a persuasive indicator that control exists.

Classification as a Consolidation or Disclosure Entity

For this illustration, management determined and the auditor concurred that, based on the assumed facts and circumstances as well as other considerations not described in the illustrations, Chatham should be reported as a consolidation entity. In arriving at this conclusion, management and the auditor considered the assumed facts and circumstances presented below in the aggregate and, finding no other facts that in the aggregate contradict these, used professional judgment to determine that Chatham is a consolidation entity.

Evidence suggesting that Chatham is a consolidation entity includes:

1. It is primarily financed by taxpayers.
2. Taxpayers have assumed the risks associated with Chatham's liabilities.

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3. Chatham's annual budget is developed by ABC officials and information related to Chatham activities is provided in ABC's performance report and Congressional Budget Justification. This indicates that decision making regarding the budget is exercised by elected officials through politically appointed officials and the budget process.

Evidence suggesting that Chatham is a disclosure entity includes:

1. Day-to-day operating decisions are made by a contractor.

After considering the above analysis and other factors, management determined and the auditor concurred that Chatham is a consolidation entity.

Administrative Assignment

ABC should consider whether or not Chatham is administratively assigned to it. In the example, evidence suggesting Chatham is administratively assigned includes ABC's role in Chatham's strategic planning, budgeting, and administration. Having considered the assumed facts and circumstances and other available evidence, the Department of ABC determined and its auditor concurred that it should consolidate Chatham's financial statements in its GPFFR.

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Gotham Laboratory

(Not included – Economic Dependency Insufficient to Show Control)

Assumed Facts and Circumstances

The Department of XYZ (XYZ), a department within the executive branch of the federal government, contracted with Gotham Laboratory (Gotham) to conduct specialized engineering research that fulfills a federal mission related to infrastructure and leads to improved services of XYZ. As specified in the agreement, XYZ provides funding to Gotham and Gotham's management team plans, manages, and executes the assigned research program.

XYZ serves on a panel providing input on the appointment of the board of directors for Gotham. However, the board of directors elects new members and the board manages Gotham's research. Gotham also may engage in any outside research activities approved by its board of directors.

Gotham performs services for various federal and non-federal organizations but receives 90 percent of its funding from XYZ. XYZ receives appropriated funds to support the Gotham research program. The remaining 10 percent of Gotham funding is derived from contracts with other federal agencies and private industry as well as donations. Gotham's budget is not reviewed or approved by any federal officials. Gotham is subject to the usual federal contract oversight and reporting requirements.

Tentative Conclusions

Based on the assumptions and other considerations, management determined and the auditor concurred that Gotham should not be included in the government-wide GPFFR. Gotham is not listed in the Budget. Further, based on the assumed facts and circumstances and other considerations, Gotham does not meet the inclusion principles of either ownership or control with expected benefits or risk of loss. Although Gotham appears to be economically dependent on the federal government, it ultimately retains discretion as to whether to accept funding or do business with the federal government. Despite the influence resulting from this dependency, the federal government does not govern Gotham's financial and operating policies.

Andromeda Prime Power Systems

(Related party- GSE)

Assumed Facts and Circumstances

The federal government created Andromeda Prime Power Systems (APPS) as a government sponsored enterprise (GSE) to facilitate commercial space travel. APPS controls interplanetary travel among a network of commercial space stations and is subject to federal regulations regarding safety and technology transfers to other nations.

APPS is governed by a nine-member board of directors elected by common stock shareholders. Board members serve three-year terms.

APPS issued common stock and received a federal government grant to finance its initial capital and startup costs. The APPS is under no obligation to return the grant funds but is expected to promote U. S. competitive interests in the emerging space travel industry.

During the reporting period, APPS' board approved a strategic plan to expand its systems to accommodate increased commercial demands and APPS issued bonds to finance the initiative. The interest rate required by lenders indicates that the market assumes the federal government has implicitly guaranteed the payment of principal and interest. In its regulatory capacity, the federal government required APPS to establish a capital reserve and created a five-member APPS Advisory Board to monitor and advise Congress on APPS' fiscal operations.

APPS derives its revenues from fees charged to commercial entities and receives no ongoing federal support through the Budget.

Tentative Conclusions

Based on the assumptions and other considerations, management determined and the auditor concurred that APPS should not be reported in the government-wide GPFFR as a consolidation entity or disclosure entity. APPS is not listed in the Budget and the federal government does not have a majority ownership interest in the company.

Further, management does a thorough assessment of control indicators and determines the federal government does not exercise control of APPS. Regulation of APPS does not, by itself, establish control.

However, based on the assumptions and other considerations, management determined and the auditor concurred that APPS should be disclosed as a related party. Related parties generally include GSEs not meeting the inclusion principles, especially those organizations that it would be misleading to exclude disclosures regarding the relationship.

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U.S. Museum (Scenario A)

(In the Budget – Consolidation Entity)

Assumed Facts and Circumstances

The U.S. Museum (the Museum) was organized to bring history and lessons about the United States to individuals through educational outreach, teacher training, traveling exhibitions, and scholarship.

The Museum is an independent establishment of the federal government and is governed by a board of trustees, known as the Museum Council. The Council has 13 voting members and 2 nonvoting members. Of the voting members, 11 are appointed by the President and serve 10-year terms (appointments are staggered) and the other 2 are appointed from among members of Congress to serve during their term. The non-voting members are selected by the Council.

The Museum receives an annual appropriation as well as private donations. Annual appropriations account for approximately 90% of operations and activities, with the remaining 10% coming from donor activities and museum sales. The museum is listed in the *Budget of the United States Government: Analytical Perspectives –Federal Programs by Agency and Account* (Budget). All donations are considered to be available for use unless specifically restricted by the donor or by time. Furthermore, the Museum is not considered to be a non-federal organization receiving federal financial assistance.

Tentative Conclusions

Based on the assumptions and other considerations, management determined and the auditor concurred that the Museum should be included in the government-wide GPFFR because the Museum is listed in the Budget (the first inclusion principle). Further, the President and the Congress appoint the Museum Council which indicates the federal government controls the Museum (the third inclusion principle).

Classification as a Consolidation or Disclosure Entity

Because it is listed in the budget, the Museum is presumed to qualify as a consolidation entity assuming no information to the contrary. In this example, management determined and the auditor concurred that there were no facts rebutting or contradicting the assumption that the Museum is a consolidation entity. As a consolidation entity, its financial statements should be consolidated in the government-wide GPFFR.

Administrative Assignment

Based on a review by management, no other component reporting entity has been assigned administrative responsibilities for the Museum. Therefore, the Museum is consolidated only directly into the government-wide GPFFR.

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U.S. Museum (Scenario B)

(Control based on Persuasive Indicator –Disclosure Entity (Financially Independent Entity))

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Assumed Facts and Circumstances

The U.S. Museum (the Museum) was organized by volunteers to bring history and lessons about the United States to individuals through educational outreach, teacher training, traveling exhibitions, and scholarship. The Museum is intended to be a self supporting operation. Shortly after its founding, it entered into a cooperative relationship with the Department of Federal Museums, a department within the executive branch.

The Museum is incorporated as a not-for-profit entity governed by the Museum Council. The Council has 15 voting members referred to as trustees. The presidentially-appointed head of the Department of Federal Museums serves as the Council chairperson. Of the remaining voting trustees, nine are appointed by the President and five are selected and approved by the Council. Except for the chairperson, all trustees serve ten-year terms which are staggered. The Council selects a Board of Directors for the Museum and appoints the Chief Executive Officer.

The Museum is a public-private partnership which receives an annual appropriation as well as private donations, rental income, and sales revenue. No fees are charged for educational events or museum tours. Rental income from the Museum facilities is derived from rates competitive with other venues for similar events. Rental of the facilities is intended to support museum activities such that the museum can eventually be self supporting. Presently, annual appropriations account for approximately 15% of operations and activities, with the remaining 85% coming from donor activities, rental income, and museum sales. The museum is listed the *Budget of the United States Government: Analytical Perspectives –Federal Programs by Agency and Account* (Budget). The funding received from donations is restricted to use by the Museum and the trustees approve the annual budget including rental income and fundraising goals.

The Museum's employees are not federal employees. The Museum is required to fully fund any deferred compensation programs and to advise its employees that the federal government has not guaranteed their deferred compensation.

Tentative Conclusions

Based on the assumed facts and circumstances and other consideration, management determined and the auditor concurred the Museum should be included in the government-wide GPFFR because it is controlled by the federal government. Although the Museum is listed in the Budget, it is a non-federal organization receiving federal financial assistance. An assessment of the remaining inclusion principles shows that the Museum is controlled by the federal government since a majority of the trustees are appointed by the President; a persuasive indicator of control.

Classification as a Consolidation or Disclosure Entity

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For this illustration, management determined and the auditor concurred that, based on the assumed facts and circumstances as well as other considerations not described in the illustrations, Museum should be reported as a disclosure entity. In arriving at this conclusion, management and the auditor considered the assumed facts and

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circumstances presented below in the aggregate and, finding no other facts that in the aggregate contradict these, used professional judgment to determine that Museum is a disclosure entity.

Evidence suggesting that U. S. Museum is a consolidation entity includes:

1. Appointments to the Council are made by elected officials.
2. Museum services are provided on a non-market basis to the general public.

Evidence suggesting that U.S. Museum is a disclosure entity includes:

1. The Museum is a separate legal entity – a not-for-profit – and terms for a majority of Council members are ten-years. This insulates the organization from political influence. Further, day-to-day operations are governed by a board of directors whose members are not directly appointed by elected officials.
2. The Museum is intended to receive limited taxpayer support and market rates are charged for facility rentals.
3. The Museum is required to make explicit that any liability for deferred compensation of its employees is not guaranteed by the federal government. This indicates that limited risks are imposed on the taxpayer.

Disclosure entities should be presented by the component reporting entity to which they are administratively assigned and, if material, by the government-wide entity.

Administrative Assignment

Management determined and the auditor concurred the Department should present the Museum as a disclosure entity in its GPFFR because the Department is assigned administrative responsibility for the Museum based on appointment of its head to serve as chairperson of the Council.

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Firefighters' Housing Limited Partnership

(Owned and Controlled - Consolidation Entity)

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Assumed Facts and Circumstances

Agency 123 has been authorized to establish pre-positioned housing and equipment storage facilities on federal land to ensure immediate and efficient deployment of fire fighting resources in response to wildfires in remote areas. The enabling legislation allows Agency 123 to enter into a wide range of financial agreements with private-sector participants to provide housing and equipment storage for the fire fighters.

The agency and a private developer formed a limited partnership—Firefighters' Housing Limited Partnership (FHLP)—to develop, operate, maintain, and own, all housing and storage units and facilities within a designated area for 25 years. Agency 123 leased land to FHLP under a 25-year ground lease. At the end of the 25-year ground lease, the agency has the option to renew the partnership for another 25 years. If it does not renew, all structures and land revert back to Agency 123, in accordance with the agency's residual ownership interest. During the 25-year ground lease, Agency 123 will provide an annual payment to FHLP from its appropriated funds for management services, use of the housing by Agency 123 employees during the fire season, and equipment storage year-round.

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The private sector partner is guaranteed a minimum payment from FHLP and has no ownership interest in FHLP properties. The private sector partner also is entitled to a share of profits from non-fire season vacation rentals of the housing so long as the facilities meet established condition requirements. Profits not distributed to the private sector partner are retained by FHLP and can be used for capital improvements including development of new housing in adjacent parks under similar terms.

As part of the partnership agreement, Agency 123 has significant authority to determine the policies governing FHLP's activities and to affect day-to-day decisions such as design and construction. Any debt incurred by FHLP must be authorized by the agency. Furthermore, capital and operating budgets require agency approval and financial transactions are monitored on a monthly basis by the agency's contract administration office. The partnership is required to produce audited financial statements annually.

Tentative Conclusions

Based on the assumed facts and circumstances and other considerations, management determined and the auditor concurred that FHLP should be included in the government-wide GPFFR. A substantial ownership interest is present via the agency's continuing ownership interest. In addition, several control indicators are met as summarized in the following analysis of available information.

1. Agency 123 may be able to direct the partnership regarding the establishment and subsequent revision of financial and operating policies through its review and approval of operating budgets, designs, and condition of the facilities. If so, this would be a persuasive indicator of control. Management should weigh the impact of its role in directing the FHLP's financial and operating policies and consider how much discretion falls to the private sector partner.

2. Other indicators in the aggregate may indicate control. Agency 123 has significant authority to:

a. direct the ongoing use of assets.

b. approve the budgets and business plans for FHLP.

c. require audits.

d. limit borrowing and investment by FHLP.

Classification as a Consolidation or Disclosure Entity

For this illustration, management determined and the auditor concurred that, based on the assumed facts and circumstances as well as other considerations not described in the illustrations, FHLP should be reported as a consolidation entity. In arriving at this conclusion, management and the auditor considered the assumed facts and circumstances presented below in the aggregate and, finding no other facts that in the aggregate contradict these, used professional judgment to determine that FHLP is a consolidation entity.

Evidence suggesting that FHLP is a consolidation entity includes the following:

1. FHLP provides housing to firefighters as its primary function on a non-market basis.
2. It is financed by taxpayer funds supplemented by any retained profits from non-fire season rentals.
3. Decisions are made by organizational leaders at Agency 123 who are appointed by the President and confirmed by the Senate.
4. Funds transferred to FHLP will be approved through the usual budgetary process so that FHLP funding will be included in the budget approved by the Congress and the President.

Evidence suggesting that FHLP is a disclosure entity includes the following:

1. FHLP has a legal identity separate from Agency 123.
2. FHLP is authorized to provide vacation housing services to customers on a market basis and use the proceeds to first compensate the private sector partner and then reduce the cost of firefighter housing borne by the taxpayer.

As a consolidation entity, FHLP's financial statements should be consolidated by the component reporting entity to which it is administratively assigned.

Administrative Assignment

Management determined and the auditor concurred Agency 123 should consolidate FHLP's financial statements because it is assigned administrative responsibility for FHLP based on its inclusion of FHLP funding in its budget request and its coordination and monitoring of FHLP's plans and performance.

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The Blue Mountain Observatory

(Control based on Indicators in the Aggregate – Disclosure Entity (FFRDC))

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Assumed Facts and Circumstances

Agency XYZ created a federally funded research and development center (FFRDC), the Blue Mountain Observatory (BMO), to provide facilities and leadership needed to conduct scientific research in a wide range of fields, including the study of black holes. Agency XYZ is BMO's primary sponsor. University Cooperative (UC) is a non-profit membership corporation created by 50 universities conducting research that would benefit from use of BMO facilities. UC was created to seek the role of managing, operating, and maintaining BMO under a cooperative agreement with Agency XYZ. UC subsequently entered into a cooperative agreement with Agency XYZ.

UC is governed by a board of trustees appointed to represent each of the 50 member universities. UC trustees appoint an individual to serve as president of BMO. The trustees also oversee BMO operations including providing input on strategic plans, approving the annual program plan before its submission to Agency XYZ for approval, responding to Agency XYZ input, and monitoring financial activities including establishing investment policies. UC employs staff to perform all BMO activities and these individuals are referred to as ‘BMO employees.’ Member universities fund any non-BMO activities of UC.

The cooperative agreement between UC and Agency XYZ ensures close coordination between Agency XYZ and BMO employees. The agreement contains requirements necessary for Agency XYZ’s oversight of both BMO’s programs and UC’s management activities, including the following provisions:

1. Provide input to a strategic plan developed by BMO employees in collaboration with UC trustees. The strategic plan sets the overall direction and priorities for BMO.
2. Agency XYZ must approve the annual program plan and budget for use of resources.
3. UC must provide to Agency XYZ an annual scientific report and audited financial statements.
4. Agency XYZ participates in developing a five-year strategic plan.
5. BMO and Agency XYZ must meet annually to review progress and ensure that scientific and facility priorities remain consistent with those of Agency XYZ.

UC works cooperatively with Agency XYZ to ensure the effective implementation of the strategic mission of BMO to the benefit of the research community. Mid-way through the current cooperative agreement, Agency XYZ will conduct comprehensive reviews of science, facilities, and management to inform future decisions regarding recompetition of the cooperative agreement for the facility. UC is under no obligation to continue in its role in managing, operating, and maintaining BMO.

In the most recent fiscal year, BMO received $100 million in funding from Agency XYZ through its cooperative agreement with UC. Agency XYZ proposed the $100 million in funding in its Congressional Budget Justification and described how the funds would be used to support the research programs at BMO. In administering the funds provided by Agency XYZ for BMO programs, UC may:

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1. expend funds to meet ongoing operational needs.
2. make annual cash contributions to employee benefits programs (accrued leave and pension plans).
3. make annual payments due under long term leases.
4. construct or purchase new assets so long as all resulting property is titled to BMO.

In the event the cooperative agreement with UC is terminated, Agency XYZ would assume management responsibility for the facility. Further, Agency XYZ would seek appropriations for termination expenses such as post-retirement benefit liabilities for BMO employees. However, Agency XYZ would be obligated to pay termination benefits only if funds were appropriated for that purpose.

Tentative Conclusions

Based on the assumed facts and circumstances and other considerations, management determined and the auditor concurred that BMO should be included in the government-wide GPFFR. BMO is not listed in the Budget so other inclusion principles must be considered. BMO facilities are owned by the federal government and new assets are titled to the federal government. With respect to the control inclusion principle, Agency XYZ establishes the fundamental purpose and mission of BMO through its participation in strategic planning and the overall effort to ensure BMO goals are consistent with Agency XYZ research goals. This effort includes annual actions to approve BMO's annual program plan and operating budget. These actions are persuasive indicators of control.

Classification as a Consolidation or Disclosure Entity

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Evidence suggesting that BMO is a consolidation entity includes the following:

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1. BMO provides, as its primary function, research facilities and leadership to university members of UC on a non-market basis. It is financed by taxpayer funds supplemented by non-government donors.
2. Key operational decisions are made by organizational leaders at Agency XYZ who are appointed by the President and confirmed by the Senate.
3. Funds transferred to BMO will be approved through the usual budgetary process so that use of taxpayer funds to support BMO is ultimately decided by the Congress and the President.

Evidence suggesting that BMO is a disclosure entity includes the following:

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1. BMO has a legal identity separate from Agency XYZ.
2. The governance structure ensures that universities have substantial input regarding BMO's strategic plans and annual program plan. The significant involvement of non-governmental entities lessens political influence.
3. BMO's liabilities are not obligations of the U.S. government.
4. BMO is authorized to accept donations from non-government entities.

Based on the assumed facts and circumstances and other information, management determined and the auditor concurred that BMO should be reported as a disclosure entity. As a disclosure entity, BMO should be presented by the component reporting entity to which it is administratively assigned.

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Administrative Assignment

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Management determined and the auditor concurred that Agency XYZ should disclose information about BMO because it is assigned administrative responsibility for BMO based on its inclusion of BMO funding in its budget request and its coordination and monitoring of BMO's plans and performance.

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Table 1: Summary Application of Proposed Standard

NAME	PAGE	IS THE ORGANIZATION INCLUDED IN THE GOVERNMENT-WIDE GPFFR?					CONSOLIDATION ENTITY OR DISCLOSURE ENTITY	
		IN THE BUDGET	OWNED	CONTROL	MISLEADING TO EXCLUDE	IS THE ENTITY INCLUDED?	A CONSOLIDATION ENTITY (CONSOLIDATED)	A DISCLOSURE ENTITY (DISCLOSED)
ABC Department	3	Yes				Yes	Entities listed in the Budget are presumed to be a consolidation entity.	
Epsilon Corporation	5	Yes				Yes	Entities listed in the Budget are presumed to be a consolidation entity.	
Sigma Association	6	No		Yes. A majority of the governing board members is appointed by the President and confirmed by the Senate.		Yes		Financially independent entity
Scholars University	8	Yes but as a non-federal organization receiving federal financial assistance.	No	No. Scholars' board of trustees elects its respective board members. Scholars' board of trustees primarily directs the university's affairs and the university seeks sources of revenue to operate virtually in a self-sustaining manner.	No	No		
Education Research Institute	10	No		Yes, the federal government can unilaterally dissolve ERI and access to its assets and responsibility for its liabilities.	.	Yes	The ERI Trust Fund is ultimately funded through taxes, elected officials establish ERI's budget, services are provided on a non-market basis, and	

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		IN THE BUDGET	OWNED	CONTROL	MISLEADING TO EXCLUDE	IS THE ENTITY INCLUDED?	A CONSOLIDATION ENTITY (CONSOLIDATED)	A DISCLOSURE ENTITY (DISCLOSED)
							taxpayers assume risk.	
Mediation, Inc.	12	Yes but as a non-federal organization receiving federal financial assistance.		Yes. Considering the control indicators in the aggregate, the federal government controls Mediation. It provides significant input on the selection of governing board members, appoints a key executive, limits Mediation's capacity to generate revenue, approves the annual budget, requires audited financial statements, and directs Mediation to work with other governments.		Yes		Mediation's governing body is insulated from political influence and risks are not assumed by the taxpayer.
Bicycle America, Inc. (Scenario A)	15	No	No. BA is owned by shareholders.	No, governing board members are elected by shareholders rather than subject to political appointment		No. BA generally provides market-based services and primarily operates independently of the federal government.		
Bicycle America, Inc. (Scenario B)	16	No	Yes, the federal government acquired 51% of the voting rights in BA.			Yes		Intervention intended to be temporary
Chatham Laboratory (FFRDC)	17	No	The assets and research results are owned.	Yes. The federal government establishes the purpose and mission of Chatham.		Yes	Yes, Chatham is primarily funded by taxpayers, and governance and accountability rests with the President and	

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		IN THE BUDGET	OWNED	CONTROL	MISLEADING TO EXCLUDE	IS THE ENTITY INCLUDED?	A CONSOLIDATION ENTITY (CONSOLIDATED)	A DISCLOSURE ENTITY (DISCLOSED)
							Congress.	
Gotham Laboratory	19	No	No	No	No	No. Although it may be economically dependent, Gotham has discretion as to whether to accept funding from the government.		
Andromeda Prime Power Systems (GSE)	20	No	No	No, APPS' governing body is elected by common shareholders. The APPS Advisory Board advises Congress and does not direct APPS' operations.		No –But Yes for related party disclosures.		
US Museum (Scenario A)	21	Yes		Yes. The Museum Council voting members, 110 are appointed by the President and 20 are appointed from among members of Congress		Yes	Yes. The Museum is in the budget and primarily funded by taxpayers and governance and accountability rests with the President and Congress.	
US Museum (Scenario B)	22	Yes but as a non-federal organization receiving federal financial assistance		Yes. The President appoints a majority of the governing body's members.		Yes		The museum is a financially independent entity.
Firefighters'	24	No	Ownership of	Yes. Agency 123 has significant		Yes	Yes. Taxpayers fund	

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Housing Limited Partnership			property is retained.	authority to direct the limited partnership's activities and to affect day-to-day activities such as in design and construction and the partnership's purpose is to carryout federal missions and objectives.			the housing and risks have been assumed through guarantee of partnership debts	
Blue Mountain Observatory (FFRDC)	26	No	Property is owned by the federal government.	Yes. The federal government establishes the purpose and mission of BMO.		Yes		BMO is a separate legal entity and UC plays a significant role in its governance without political influence.

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